STATEMENT

of

Teresa Bryce

On

Title V

H.R. 1295

"The Responsible Lending Act of 2005"

before the

Subcommittee on Housing and Community Opportunity

Committee on Financial Services

United States House of Representatives

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Good morning, and thank you Mr. Chairman, for holding this hearing and inviting the Mortgage Bankers Association (MBA)[1] to share its views on Title V of H.R. 1295, "The Responsible Lending Act of 2005." My name is Teresa Bryce and I am Senior Vice President and Director of Legal and Corporate Affairs for Nexstar Financial Corporation, a mid-size mortgage banking company located in St. Louis, MO. I am also Co-Chair of MBA's State Licensing Task Force, formed last year to review the impact that the myriad of new state licensing laws are having on mortgage bankers. MBA is particularly interested in testifying today because state licensing laws have become an issue of growing concern among mortgage bankers as we work to be the efficient financial link between homebuyers and capital markets.

Title V of H.R. 1295, "Requirements For Mortgage Brokers," mandates that states pass uniform statutes for the licensing of mortgage brokers, creates Federal mortgage broker requirements for those states that do not pass compliant legislation, and establishes a national database of licensed mortgage brokers that would be accessible by state and federal regulators, real estate finance companies employing mortgage brokers, and the general public.

MBA supports Title V because we believe it will elevate the standard of professionalism within the mortgage broker industry. Title V will also result in greater accountability among mortgage brokers while at the same time easing the compliance problems caused by different state laws for mortgage brokers who broker in multiple states. MBA would suggest some changes to Title V that would serve to strengthen the legislation.

Before I outline MBA's support for Title V and detail our suggested changes, I would like to give the subcommittee some background on the mortgage banking industry and MBA's particular interest in mortgage banker and broker licensing laws.

<u>What Mortgage Bankers Do</u>

Mortgage bankers provide mortgages to homeowners and homebuyers. Mortgage bankers underwrite applicants and lend their own funds or funds they have borrowed in a mortgage transaction. From the moment a loan has closed, mortgage bankers assume the credit, interest rate, compliance, and fraud risk associated with the loan.

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[1] **The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 500,000 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 2,900 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.**

Mortgage bankers may then service and/or sell these closed loans to the secondary market. If a loan is sold, the mortgage banker typically transfers the future interest rate and credit risk to the investor, but maintains nearly all of the quality, compliance, and fraud risk.

In the above manner, mortgage bankers are truly financial intermediaries that bring together providers of capital (investors) and those needing such funds (homebuyers) in all regions of the country. This function moves funds from capital-surplus areas to capital-deficient regions, and helps create jobs and economic growth throughout the nation.

Mortgage bankers are organized in many forms: Federal- and state-chartered banks, thrifts, credit unions, and other depository institutions, as well as non-depository mortgage companies. Mortgage bankers also come in many different sizes, from small businesses to large multi-national corporations. Mortgage bankers use an array of methods in connecting consumers with capital: traditional branch offices, the U.S. mail, call centers, and the internet.

Mortgage bankers face several levels of regulatory oversight depending on how they are organized. Federal- and state-chartered depository institutions are regulated by the appropriate Federal or state banking agency. In 49 states and the District of Columbia, non-depository mortgage companies are licensed and regulated by state regulatory agencies. Fannie Mae, Freddie Mac, and the Federal Housing Administration (FHA) approves and oversees any mortgage banker who wishes to work with them. Additionally, private investors and mortgage insurance companies conduct audits of the lenders with whom they work.

Regardless of their internal structure, all mortgage bankers face economic regulation through the mortgages they keep in their portfolio and the mortgages they sell to investors.

If a mortgage bank retains a mortgage in its portfolio, it is relying on the continued performance of that mortgage in order to realize a profit. In this case, the mortgage bank bears the full risk of the loan.

Alternatively, if a mortgage bank sells a mortgage, the bank makes certain representations and warranties to the investor. If the investor discovers problems, such as non-compliance with applicable law or underwriting guidelines, or fraud, the investor can, and typically does, force the originating mortgage banker to repurchase the mortgage or enter into an indemnity agreement. Investors, such as the Government Sponsored Enterprises (GSEs) and private institutions, therefore, pay strict attention to the operations of the mortgage bankers from whom they purchase loans.

In this manner, mortgage banking companies are corporately responsible for every loan originated by any of their employees, and this economic regulation by the marketplace extends far beyond the loan closing.

What Mortgage Brokers Do

Mortgage brokers, on the other hand, do not fund, underwrite, or service mortgage loans. Mortgage brokers are commissioned sales people, independent of mortgage banking companies, who typically work with a number of mortgage bankers at any one time, matching homebuyers with lenders.

Mortgage brokers do not have capital at risk in a transaction and their responsibility for a loan typically ends when a loan closes and they receive their payment. In most cases, mortgage brokers operate with considerably fewer assets than mortgage bankers. In those states where mortgage brokerage companies are licensed, minimum financial requirements on these firms tend to be significantly less than mortgage bankers.

Lenders have little expectation of recovering losses from brokers and typical recourse is to simply no longer do future business with the broker. While this may prevent future losses, it does nothing to address the risks or costs that the existing portfolio of loans received from that broker imposes on the mortgage banker.

There is no Federal oversight of mortgage brokers. Since mortgage brokers do not sell mortgages on the secondary market, there is little marketplace regulation.

The Difference Between Mortgage Bankers and Mortgage Brokers

While the entrepreneurial spirit of the mortgage banking industry has created the sophisticated and innovative real estate finance system that the U.S. enjoys today, a key difference between the mortgage broker, (which is the subject of Title V's requirements), and the mortgage banker has remained the same despite the changes in the system. This key difference is that, at some point in the transaction, mortgage bankers, unlike mortgage brokers, have money at risk and must continually maintain a significant amount of financial wherewithal to back up the loans they sell.

This is evident in the requirements that investors such as Fannie Mae and Freddie Mac place upon mortgage bankers who wish to sell loans to them. It is also evident in the state statutes that have been promulgated to regulate mortgage banking companies and mortgage brokers: typically, mortgage bankers are expected to attain and retain a much higher financial and professional profile.

Another difference between mortgage bankers and mortgage brokers is the relationship to the consumer. Mortgage bankers typically offer their own financing products to consumers and do not present themselves as operating on behalf of the consumer. Mortgage brokers, on the other hand, present themselves as specifically acting in the interest of the consumer by shopping on behalf of the consumer for the best product that meets the consumer's needs and financial circumstances. Mortgage broker commissions are fundamentally based on this service offer.

MBA is aware of case law that has found fiduciary relationships in many mortgage broker-client relationships, but that the mortgagor-mortgagee relationship does not create a fiduciary relationship, as a matter of law. In the unregulated or under-regulated mortgage brokerage business, it is prudent for regulators to step in and license those individuals who have a fiduciary relationship with a consumer.

This is exactly why MBA supports Title V. We believe Title V will elevate the standards within the mortgage brokering industry and lead to greater accountability. The National Association of Mortgage Brokers (NAMB) recognizes the need for licensure among their members and has created a model state statute that would result in all mortgage brokers being licensed. Many states have likewise identified the need to imbue greater professionalism and accountability within the mortgage brokering industry and have passed laws that require licensing of individuals working as mortgage brokers.

The Current State Licensing Environment

Despite the fact that today's hearing is focused solely on mortgage broker licensing, I would like to take a moment and give the subcommittee an overview of the current licensing environment for mortgage bankers at the state level and the difficulties it is imposing on them. I believe there are lessons to be learned from the state level experience as this subcommittee considers Title V.

States have traditionally licensed mortgage banking companies as a means to monitor the mortgage lending industry in their state, prevent abusive lending, and protect consumers' interests. Licensing also provides states with revenue, which is derived from the various fees charged to obtain and maintain a license, and is often used to fund oversight activities. Currently, 49 states and the District of Columbia require mortgage bankers (who do not enjoy a federal pre-emption) to be licensed before lending funds in their state.

MBA supports state level corporate licensing of mortgage banking companies. We believe that states should be able to approve and monitor the companies that make loans to citizens within their state. And while we may, from time to time, take issue with a particular provision under a state's corporate licensing regime, we do not believe a state should be limited from knowing which mortgage banking companies are lending within their boundaries.

In conjunction with these licensing laws comes regulation by state executive agencies. This oversight takes many forms, but often includes annual reviews of financial statements, onsite reviews of operations, recertification of company principals, and requests for responses to consumer complaints.

In recent years, however, a growing number of states have added onerous requirements to existing mortgage banking company licensing. For instance, more and more states have begun to require mortgage banking companies to maintain an employee or branch physically in the state to take applications. This requirement may unduly restrict lenders who centralize applications in a call center or utilize technologies such as the internet. Furthermore, this requirement is likely a violation of the Interstate Commerce clause of the United State Constitution. Some states inexplicably require a physical branch with an employee in the state but do not require that loan applications be taken from the state branch. Other states require separate licensing for mortgage brokering, even if a company already has a mortgage banking license. Still other states require separate licensing for different mortgage products.

Particularly arduous, though, are the states that have moved beyond mortgage banking corporate licensing and now require the licensure of individual loan officers and support staff working within a licensed mortgage banking company. These state statutes ignore the accountability that mortgage banking companies have for their loan officers and employees due to the economic regulation of the marketplace and the periodic audits by the states themselves. These state statutes do not recognize the rigorous background checks, continuous training, and ongoing performance monitoring, that mortgage banking companies put their loan officers through due to the economic regulation to which mortgage banking companies are subject.

These laws are being promulgated with an out-dated view of the mortgage origination process and do not recognize the various channels today's sophisticated residential real estate finance system has available to it in transferring national and international capital to homebuyers anywhere in the country. Collectively, these state laws raise costs of mortgage originations and threaten to dampen competition and innovation of mortgage markets within states.

Further exacerbating the collective impact of these various state laws is the lack of reciprocity provisions. This lack of reciprocity results in great redundancies. For instance, a state's reasonable requirement that a mortgage banking company's principal submit their fingerprints does not account for the fact that the same principal is submitting their fingerprints to a dozen or more other states and they all end up at the FBI. These same principals might be required to take 12 hours of continuing education annually in multiple states, without any state recognizing the education received elsewhere. As states require loan officer licensing, the lack of reciprocity means that loans officers would have to submit to multiple and redundant pre-licensure training, exams, background checks, and continuing education requirements. This is beginning to create an untenable situation for mortgage banking companies.

The situation is made worse by the inadequate funding these state agencies receive to process licensing applications with increasing onerous requirements. Despite this under-funding, the mortgage banker is required to hire a person before they can be licensed and then have them on the payroll for lengthy periods before they can perform the job they were hired to do while, the state is slowly processing the individual's licensing application.

It is important to note, that federally-chartered financial institutions that originate mortgages are considered exempt from all of these state laws and therefore do not share these problems.

Simply put, MBA believes mortgage bankers are different than mortgage brokers and these differences underscore the need for mortgage bankers and mortgage brokers to be subject to different oversight regimes. Unfortunately, MBA does not see this difference being reflected in licensing laws affecting mortgage bankers being promulgated at the state level.

Organizations such as the Conference of State Bank Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR) have recognized the problems imposed by the growing patchwork of state licensing laws and are trying to create solutions to lessen the burdens, such as creating a universal licensing application and a common database of licensees. MBA has been involved in these efforts and is very supportive.

While we believe the efforts of CSBS and AARMR will have some beneficial results, we are concerned that their effort to streamline licensure and encourage uniformity will be ultimately stymied as they confront state laws that contradict each other, lack reciprocity and ultimately confound conformity.

<u>What Title V Will Do</u>

While states have a relatively long history of requiring licensure of mortgage banking companies, the same is not true for the mortgage brokerage industry. Mortgage brokers are not regulated at the Federal level and it is only recently that the majority of states begun to require licensure. This industry is in great need of licensure and Title V offers an opportunity to do this in a reasonable manner. Mortgage brokers regularly state in their literature that they are involved in nearly 70% of residential mortgage loans originated.

The database created by Title V has the potential to be a great resource to regulators, mortgage bankers, and the public. Currently, no single database of mortgage brokers exists, and it is not necessarily easy to access the data in those states with mortgage broker licensing laws. With the rising tide of mortgage fraud against lenders, mortgage bankers have called for better tools that allow for sharing the names of “bad actors” who are defrauding homebuyers and lenders, without the fear of legal action that to date has accompanied such sharing of information. The database contemplated by Title V could go a long way in furthering such information sharing.

Appraisers, who are licensed and regulated at the state level, have such a database managed by the Congressionally-appointed Appraisal Subcommittee. The database includes actions taken against appraisers and is accessible through the internet by the general public.

What Title V Will Not Do

Unfortunately, though, Title V will do little to help mortgage bankers manage the thickening web of burdensome state licensing laws, particular those laws that do not recognize how the modern residential finance system operates and requires the licensure of individual loan officers.

Under Title V, states must adhere to uniform standards of mortgage broker licensing laws, but are not prevented from continuing to pass laws requiring the licensing of individual loan officers of mortgage banking companies.

Therefore, the subset of the mortgage banking industry that is subject to these laws must continue to operate in an uneven competitive field that is increasingly uneven. Some mortgage banking companies may restructure under a Federal-charter so as to avoid such strict licensing regime, as the Federal banking agencies do not require licensure of individual loan officers. The mortgage banking entrepreneurial spirit will thus be somewhat constrained, not by the realities of the marketplace, but by the force of duplicative regulation.

MBA supports the licensing provisions under Title V, as we believe they will elevate and standardize the mortgage brokerage licensing requirements. MBA encourages the committee to study possible federal initiatives that will assist mortgage bankers when dealing with state level corporate licensing laws.

Improvements to Title V

MBA is aware that some have criticized the exceptions to licensing contained within Title V, stating the exceptions provide too many loopholes where an individual could easily avoid licensure, despite the fact that their primary business is mortgage brokering.

MBA suggests the subcommittee consider elaborating upon the exemption cited in Section 501 (b)(2)(F)(i) to make it clear that by “makes, services, buys, or sells mortgage loans;” the statute is clearly exempting those firms that fund the loan, a key distinction between mortgage banker and mortgage broker that I detailed earlier in my testimony. By clearly excluding mortgage banker, the statute will be clearly including all mortgage brokers. The subcommittee may wish to examine the exemption under Section 501(b)(2)(F)(i)(iii)(V), to ensure that it does not establish such a low threshold as to allow a mortgage broker an easy way to avoid licensure.

Creating statutes that appropriately license mortgage bankers and mortgage brokers can be, at times, a complex issue. MBA is grappling with this complexity with regard to state legislation and strives to be a source of information as to how states can effectively provide oversight, without constraining markets.

Likewise, we want to be a resource to this Subcommittee on Title V and are willing to work collectively, with all interests in the real estate finance system, to create oversight mechanisms that elevate accountability, but not at the expense of efficient markets nor accompanied by the price tag of greater complexity.

MBA appreciates the opportunity to testify today. We look forward to working with this Subcommittee in creating a strong mortgage broker licensing requirement.