Comments submitted by the
Center for Responsible Lending[1]
To the Consumer Financial Protection Bureau

RE: Truth in Lending Act (Regulation Z)
Loan Originator Compensation

Docket No. CFPB-2012-0037
RIN 3170-AA13

October 16, 2012

Thank you for the opportunity to comment on the Consumer Financial Protection Bureau's (CFPB) proposed rule regarding loan originator compensation. The limits on loan originator compensation contained in the Dodd-Frank Wall Street Reform and Consumer Protection Act and in Regulation Z are important consumer protections that fundamentally improve the mortgage market and reduce the incentives that mortgage originators have long had to benefit themselves financially by placing borrowers in worse loans than they qualify for. As explained in detail below, our comment focuses on the following:

1) If the CFPB allows individual loan originators to participate in bonus and profit-sharing plans of their employer, it should only in limited circumstances with restrictions;
2) CRL supports the CFPB's use of its exception authority to allow a loan originator to charge upfront origination and/or discount points and receive compensation from a source other than the borrower, given the other consumer protections that will remain in place;
3) CRL does not believe that requiring a lender to provide borrowers with a loan option that has no upfront points or fees will provide enough protection to outweigh the potential harm to consumers and lenders alike; and
4) In lieu of the zero-zero option, CRL suggests that lenders should be required to disclose all points and fees charged when they give a quote to a borrower to provide consumer protections and allow lenders to compete fairly in the marketplace.

1) Bonus and Profit-Sharing Plans

If the CFPB allows individual loan originators to participate in bonus and profit-sharing plans of their employer, it should only in limited circumstances with restrictions. Thus, CRL believes the bar should be set at 25% of overall revenue rather than 50%. The larger the percentage of revenue derived from a company's mortgage lending unit, the more opportunity exists for the mortgage unit to skew the results of the overall bonus or profit-sharing plan. As such, the pressure on the mortgage lending operation to

[1] The Center for Responsible Lending (CRL) is a not-for-profit, non-partisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, one of the nation's largest nonprofit community development financial institutions. Self- Help has provided $6 billion in financing to 70,000 homebuyers, small businesses and nonprofits and serves more than 80,000 mostly low-income families through 25 retail credit union branches. Additionally, Self-Help has originated $387 million of home loans and financed $4.7 billion in loans to low-income families that Self-Help purchased from lenders across the country under Self-Help's home loan secondary market program.

boost revenues is increased, which in turn creates incentives to steer borrowers into more expensive loans. Revenues from affiliates should count toward overall company revenue.

If companies are allowed to exclude revenues from affiliates in the overall total, then companies seeking to evade the limit on revenue will have an incentive to shift their mortgage lending operations into affiliates. All affiliate revenue should count toward the total to adequately capture the true impact of mortgage lending operations on the company's revenue.

2) Use of Exception Authority to Permit Loan Originator Compensation When Upfront Points and Fees Are Charged

CRL supports the CFPB's use of its exception authority, which would permit loan originators to receive compensation from a source other than the borrower when upfront origination points or discount points are charged. The use of origination fees and discount points to reduce the interest rate for a loan can provide value to the borrower in certain circumstances. These fees are common in the prime market, the basis for this exception is specifically included in the Dodd-Frank Act,[2] and protections regarding fees in the Dodd-Frank Act will remain in place. These protections include:

- No compensation that varies based on the terms of the loan;[3]
- No split payments from the consumer and loan originator;[4]
- The three percent points and fees limit for qualified mortgages;[5]
- The five percent points and fees threshold under HOEPA;[6]
- The significant restrictions on prepayment penalties;[7]
- The ban on financing single premium credit insurance;[8] and
- The Loan Estimate form, including listing settlement charges, as part of the proposed revised TILA/RESPA disclosures.

Past abuses with upfront fees were most significant in the subprime market and before these substantive protections were in place. Given those changes, we believe this exception would not pose undue risk for consumers. However, fees have long been an area of abuse in mortgage lending, so we would encourage the CFPB to closely monitor this practice to ensure that consumers are not being subject to inappropriate charges and adjust as necessary.

3) Zero-Zero Option Requirement

We do not believe that requiring lenders to offer a product with no upfront origination fees or discount points would provide significant protections to borrowers, would likely be confusing, and could also harm lenders. Further, the complexity discussed in the proposed rule also argues against requiring that this option be offered.

[2] 15 USC 1639b(c)(2)(B).
[3] 15 USC 1639b(c).
[4] *Id*.
[5] 15 USC 1639c.
[6] 15 USC 1601, 1639.
[7] 15 USC 1639c(c).
[8] 15 USC 1639c(d).

Whether the borrower receives a zero-zero offer first depends on whether the lender can offer an option for which the borrower can qualify. Determining whether this will be the case or not may be confusing for both lender and borrower. If the borrower does qualify for that product, then the borrower still must understand the trade-off between points and rate. While the zero-zero option offered by a particular lender may be less complicated than other options that lender offers, it may not be the best deal for the consumer. For instance, the borrower may think that the pricing on a zero-zero option by a particular lender is indicative of the pricing offered by that lender of the option with upfront fees. However, one lender may price the zero-zero option at a much higher interest rate in part to discourage borrowers from actually taking the offer. If a second lender prices their zero-zero option at a lower interest rate, then the borrower may assume the second lender's product with upfront fees is perhaps less expensive that the first lender's product, even if that is not the case. And, as alluded to in the proposed rule, lenders would be discouraged from making the case to the borrower that a zero-zero option is less advantageous, even when it really is.

The CFPB recognizes in the proposed rule that lenders may face difficulty in making a zero-zero option available. For secondary market transactions, there is not a linear relationship between price and yield, and the relationship varies with market conditions. Thus, for lenders that sell loans on the secondary market, investors at times may not be willing to pay a sufficient premium for higher interest rate loans to permit the lender to recoup its origination costs due to prepayment risk. As a result, lenders may find it cost-prohibitive to offer zero-zero option loans, especially for smaller lenders or on smaller loans.

In addition, as the Bureau also recognizes in the proposed rule, portfolio lenders would not be able to recoup origination costs upfront, leaving these lenders at a greater risk of not being reimbursed for the costs incurred in making the loan through early prepayment. As a result, portfolio lenders may be forced to price their zero-zero options at a greater interest rate premium than lenders who sell their loans on the secondary market, which would put portfolio lenders at an unnecessary disadvantage.

Further, lenders are limited in how much can be added to the interest rate before triggering higher-priced mortgage loan (HPML) limits on the state and federal level, which trigger additional protections and reporting requirements. For instance, federal protections for HPMLs include mandatory escrow accounts, appraisal requirements, and reporting under HMDA.[9] Once the loan becomes an HPML, it becomes a much more complicated product that many smaller lenders would not be able to offer.

Finally, the complexity the Bureau cites in the proposed rule further underscores the point that the benefit to consumers does not outweigh the potential costs. For example, the Bureau notes that APRs on the zero-zero option will vary for loans with fees paid to affiliates versus loans without affiliate fees. As a remedy, the proposed rule discusses the possibility of an exclusion for what would be defined as "ancillary services" while leaving "core loan origination services" included. This kind of complexity would further complicate the process and may mislead consumers about the fees being paid through the interest rate.

Helping borrowers understand the rate-fee trade-off would be preferable. With the improvements discussed above that Dodd-Frank provides, and the changes to the RESPA and TILA disclosures are

[9] 12 CFR 226.35.

finalized, then the borrower is in a better position to compare offers and weigh different options accordingly.

4) Alternative Requirement

In lieu of the zero-zero requirement, CRL suggests that the Bureau require lenders to include *all* fees that a lender charges that are included in the definition of "discount points, origination points, or fees," including fees paid to affiliates, when providing a quote to a borrower. This amount disclosed would be the same as the finance charge the Bureau uses to calculate the Transaction Coverage Rate in the RESPA/TILA proposed rulemaking. This requirement would be helpful, since, for example, a lender may disclose an origination fee while also planning to charge the borrower "junk fees", such as commitment, underwriting or processing fees.

If a lender is only required to disclose certain fees to the borrower, then some lenders would simply shift their compensation to other fees that the borrower would only learn about later in the process. As the CFPB notes in the proposed rule, funds derived from different fees are fungible. As such, a lender who discloses all fees would seem to have a more expensive product than another lender, even though this is not the case. This requirement would ensure effective competition early in the process.

We would also recommend that the CFPB not require demonstrating the yield trade-off on upfront fees, which is a broader and different inquiry than how to define bona fide discount points for exclusion from the points and fees limits for qualified mortgage and HOEPA. In that case, the statute explicitly refers to "bona fide" discount points that can be excluded in certain situations, which would require the Bureau to establish a test that there is a real interest rate reduction. However, in this case, since upfront fees are common with mortgage loans and the protections discussed above from Dodd-Frank are present, there is less need to engage in the complexity needed for this inquiry on all loans.

For additional information or to ask questions about this comment, please contact Eric Stein (eric.stein@self-help.org) or Chris Kukla (chris.kukla@responsiblelending.org).