CENTER FOR RESPONSIBLE LENDING

Overbroad Exemptions to the QM limits on points and fees make mortgages more expensive and less safe.

Fact Sheet *April 13, 2015*

Proposals to exempt affiliated title insurance from the Qualified Mortgage (QM) points and fees limits are costly, dangerous, and unnecessary for borrowers. The market is slowly recovering, even if unevenly. Initial reports show that there is little or no evidence to show that the rules were having a significant impact. Reports by Federal Reserve's Senior Loan Officer Survey show that the majority of respondent loan officers did not note negative impacts from the QM rule.[1]

For consumers, the title insurance market is anti-competitive and expensive. Exemptions from the QM rules incentivize steering and fee packing, and make a broken market worse.

- In 2007, a GAO report concluded that borrowers "have little or no influence over the price of title insurance but have little choice but to purchase it." As a result, the fees are grossly inflated—recent studies have found that 70 cents of every premium dollar for title insurance goes to commissions, whereas 5 cents to 11 cents goes to paying claims.[2]
- Anti-competitive practices put companies that market directly to consumers and can offer lower rates at a significant disadvantage. One such company, Entitle Direct, has roughly .1% of the market despite having fees that are often 35% less than the competition. One expert explained that the challenge is, "the limited price competition in title insurance markets and the strength of the institutional arrangements between title insurers and those able to steer title business — lenders, developers, Realtors, builders…"[3]
- The points and fees definition for QM loans is designed to include all compensation received by the lender. It is a reasonable standard (with small loan exemptions) that provides basic protections for homebuyers.

Lifting points and fees caps is especially inappropriate given the limited state or alternative federal oversight of the title insurance industry. The rules level the playing field.

- A 2010 study from the National Association of Insurance Commissioners regarding state regulation of title insurance reports that half of all states either do not regulate title insurance rates or allow insurers to set their rates and essentially notify state regulators.[4]
- A small handful of states do adequately review rates to prevent price gouging, but more than half have "file and use" or "use and file" rules. In these states, insurer rate schedules often go into effect after a specified number of days unless the regulator intervenes. In many of these instances, the regulator is not required to respond and, in practice, they rarely do. Another group of states only require that the rates be "reasonable," or do not regulate title insurance at all.[5]
- While the federal Real Estate Settlement Procedures Act (RESPA) prohibits paying kickbacks to third-party title agents, the law does not prohibit payments to affiliated title firms. This rule incentives a title agency to be affiliated so it can gain the payment option without violating RESPA.[6] The points and fees cap simply levels this playing field between affiliated and unaffiliated title insurance companies.

Without today's appropriate market incentives and consumer protections, borrowers will pay the price in hundreds if not thousands of unnecessary costs.

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[1] BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, JANUARY 2015 SENIOR LOAN OFFICER OPINION SURVEY ON BANK LENDING PRACTICES 37 (2015), *available at* http://www.federalreserve.gov/boarddocs/snloansurvey/201502/fullreport.pdf.

[2] U.S. GOVERNMENT ACCOUNTABILITY OFFICE, TITLE INSURANCE: ACTIONS NEEDED TO IMPROVE OVERSIGHT OF THE TITLE INDUSTRY AND BETTER PROTECT CONSUMERS 53 (2007), *available at* http://www.gao.gov/new.items/d07401.pdf.

[3] Lisa Prevost, Saving on Title Insurance, New York Times (March 14, 2013), *available at* http://www.nytimes.com/2013/03/17/realestate/saving-money-on-title-insurance.html?_r=0.

[4] NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS TITLE TASK FORCE, SURVEY OF STATE INSURANCE LAWS REGARDING TITLE DATA AND TITLE MATTERS 8 (2010) *available at* http://www.naic.org/documents/committees_c_title_tf_survey_state_laws.pdf.

[5] Joyce D. Palomar, Title Insurance Law: Chapter 18 State Regulation of Title Insurance, 2 Title Ins. Law § 18:17-22 (2014-2015ed.)

[6] 12 U.S.C. 2607(c)(4), as amended.

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Maintain Safegards that Protect Buyers of Manufacted Homes

Fact Sheet *April 13, 2015*

Manufactured homes can be an important affordable housing option for families. This is especially true in many rural areas of the country where rental units are scarce and more traditional housing is out of reach for low and moderate-income households. Current rules protect owners of manufactured homes by limiting opportunities to take advantage of those who can least afford it. According to a recent exposé by the Pulitzer Prize winning investigative journalism group the Center for Public Integrity in partnership with the Seattle Times, the nation's largest builder of manufactured homes:

> *"relies on predatory sales practices, exorbitant fees, and interest rates that can exceed 15 percent, trapping many buyers in loans they can't afford and in homes that are almost impossible to sell or refinance…."*[1]

The current rules already accommodate differences in the manufactured housing market. Weakening rules would further incentivize bad behavior and harm consumers.

- Currently, borrowers who sign high-cost loans get Home Ownership and Equity Protection Act (HOEPA) protections if the loan has points and fees totaling:
  - The lesser of 8% of the loan amount or $1000 for loans under $20,000; and
  - 5% of the loan amount for larger loans.
  - For instance, for the average manufactured home loan of $67,500, these HOEPA protections are triggered when a borrower pays $3,375 in fees.
- The current HOEPA interest rate cap is 8.5% for loans less than $50,000. At a time when borrowers are receiving historically low interest rates, there are proposals to allow manufactured housing loans with as much as 14% interest rates to escape certain consumer protections.

A new emerging secondary market for these loans makes it all the more important to keep reasonable protections in place.

- The Federal Housing Finance Agency (FHFA) is required by law to establish duty-to-serve rules to stimulate GSE investment in certain manufactured housing loans.
- A new secondary market may reduce lenders' 'skin in the game' making it all the more important to keep appropriate protections in place.
- High cost loans sold onto the secondary market without proper rules in place to measure affordability laid the foundation to the housing crisis. Even if on a smaller scale, relaxing common sense rules is a recipe for disaster.

Bans on incentivizing kickbacks and steering are appropriate.

- Compensation for steering borrowers into high cost loans is already barred in other mortgage products. There is no reason to allow costly and discriminatory behavior in this market.
- The Proposed changes do not provide clarification. They instead offer dangerous and unnecessary changes to allow kickbacks for steering borrowers into higher priced loans.

Industry data suggest the market is doing well under the rules.

- Production of manufactured homes in January 2015 was 14% higher than in January 2014, continuing the trend of robust growth.
- Berkshire Hathaway recently reported that its Clayton Homes, the largest builder, retailer and lender, saw pre-tax earnings grow by 34% in 2014.

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[1] *Available at* http://www.seattletimes.com/business/real-estate/the-mobile-home-trap-how-a-warren-buffett-empire-preys-on-the-poor/

Additional QM Carveouts for Portfolio Loans Held by Larger Banks Add Excessive Risk to the Market

Fact Sheet *April 13, 2015*

Holding loans in portfolio alone will not protect borrowers, taxpayers, and the market from the mistakes of the past.

- In the lead up to the financial crisis, many of the toxic loans, such as negative amortization loans, and adjustable rate mortgages ("ARMs") underwritten to initial "teaser" rates were held in bank portfolios. Lenders underwrote these loans based upon only this initial, artificially low payment, even though dramatically higher payments kicked in after a few years.
- Many lenders did not document the income of the borrowers, instead making no documentation ("no-doc") loans. Hundreds of billions of dollars of these loans were made, and many were kept on bank portfolios. These loans soon crashed, helping to trigger the financial crisis, and devastating banks such as Washington Mutual and Wachovia.[1]

Automatic Qualified Mortgage (QM) status to loans held portfolio should not be extended to larger institutions.

- Under the current rule, small and rural lenders can hold loans in portfolio with QM status as long as they have considered and verified a borrower's debt-to-income ratio although they do not have to limit DTI to 43% as required for loans sold in the secondary market.
- Portfolio loans can still be risky for consumers and taxpayers. Many homeowners have very substantial equity in their homes and a significant number of those have no current home debt. Current information shows that the average loan-to-value for GSE loans is 75% with many loans having much lower levels. With these loans, the borrower's equity absorbs the risk of loss rather than the lender. Therefore, the lender is protected even from very risky loan terms.
- Granting QM status to portfolio loans held by larger financial actors will allow some to use relaxed standards to harm consumers and strip consumer equity, all while being insulated by QM's legal protections.
- While no changes are necessary, if any additional QM portfolio loan exemptions are granted, rules must ensure that lenders have an actual incentive to avoid risky and unnecessarily expensive products.

Even measures that require holding periods before a loan gains QM status pose significant risks to borrowers.

- Time limited portfolio exemptions that have been proposed do not prohibit an institution from selling the loan before the time period without losing the QM designation.
- For instance, a three-year limit on holding loans in portfolio could result in larger institutions creating loans that reset to unsustainable levels when that limit has expired, yet also maintain QM status with legal protections.
- Recent experience clearly demonstrates that these types of unsustainable toxic products are harmful for many consumers. Policies that open the door to returning to the recklessness of the past put consumers and the greater economy at serious risk.

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[1] Ben White and Eric Dash, Wachovia, Looking for Help, Turns to Citigroup, New York Times (September 26, 2008), *available at* http://www.nytimes.com/2008/09/27/business/27bank.html?_r=0.

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Appraisal Requirements Protect Consumers from Abuses in Mortgage Lending

Fact Sheet *April 13, 2015*

Appraisal requirements protect consumers from abuses in mortgage lending and help to ensure the borrowers can repay their mortgage loans.

- The Dodd-Frank Act and the Consumer Financial Protection Bureau have improved appraisal-reporting standards. The new rule enacted in 2014 requires that applicants receive copies of all appraisals and home value estimates.[1] The rule also allows for consumers to receive information on how the property was evaluated in advance of closing.
- In addition, rules for certain higher risk mortgages[2] now require lenders to use a licensed appraiser who reports on the physical inspection of the inside of a home, and requires that lenders disclose the purpose of the inspection, and provide a free copy of the appraisal report.
- The term "higher-risk mortgage" refers to subprime-like mortgages -- loans that are made at higher than prime market rates and generally include other high-risk features that resulted in unsustainable loan products that devastated homeowners across the nation.
- The rules help to ensure that mortgage loans are properly and accurately collateralized. This protects both the lender, through adequate collateral for their loan, and the borrower, by preventing them from borrowing more than their home is worth.

Rolling back appraisal standards and reporting requirements will take us back to the period of misconduct that contributed to the housing crisis.

- Proposals to exempt banks from fulfilling appraisal requirements for "higher-risk" or any loans under $250,000, would mean that almost half of all new homes sold in the United States could be exempt from appraisal standards reporting requirements.
- In the lead up to the financial crisis consumers suffered from intentional inflation of home appraisals. The Financial Crisis Inquiry Commission cites various testimonies describing the prevalence of fraudulent appraisal practices in the lead up to the housing crisis. This practice, extremely harmful on its own, also proved to be a dangerous combination with declining incomes and toxic loan products.[3]

Congress should not support legislation that removes this consumer protection and should uphold appraisal rules, which help to ensure a safer transaction for both the homeowner and the lender.

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[1] Rule *available at* http://files.consumerfinance.gov/f/201301_cfpb_final-rule_ecoa-appraisals.pdf.

[2] Board of Governors of the Federal Reserve System (Board); Consumer Financial Protection Bureau (CFPB); Federal Deposit Insurance Corporation (FDIC); Federal Housing Finance Agency (FHFA); National Credit Union Administration (NCUA); and Office of the Comptroller of the Currency, Treasury (OCC). *available at* http://files.consumerfinance.gov/f/201301_cfpb_final-rule_tila-appraisals.pdf.

[3] FINANCIAL CRISIS INQUIRY COMMISSION, THE FINANCIAL CRISIS INQUIRY REPORT 16, 43 (2011), *available at* http://fcic.law.stanford.edu/report.