CSBS SINCE 1902
CONFERENCE OF STATE BANK SUPERVISORS

October 16, 2012

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Dear Ms. Jackson,

The Conference of State Bank Supervisors (CSBS) appreciates the opportunity to comment on the Consumer Financial Protection Bureau's (CFPB's) proposed rule entitled *Loan Originator Compensation.* In the proposed rule, we believe the CFPB has appropriately evaluated existing standards for loan originator compensation and new Dodd-Frank mandates related to upfront points and fees and provided helpful clarification and flexibility in these areas. Our analysis focuses on the CFPB's proposals related to restrictions on upfront points and fees and loan originator compensation.

RESTRICTION ON UPFRONT POINTS AND FEES

As written, section 1403 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) prohibits consumers from paying upfront points or fees to mortgage loan originators (MLOs), creditors, or their affiliates in all retail and wholesale loan originations where creditors or brokerage firms compensate MLOs (i.e., where there is creditor-paid compensation or brokerage-paid compensation). Section 1403 gives the CFPB authority to waive this mandate or provide exceptions if it is in the interest of consumers or the public.

It is important to note that the upfront fees addressed in this proposal are not fees paid in advance of closing, or those typical of advance payment schemes. The fees under consideration are discount points or origination points or fees agreed to at closing by the consumer and the creditor. Discount points are paid by consumers to the creditor to purchase a lower interest rate. Creditors and/or loan originators also sometimes charge origination points or fees, which are typically presented as charges to apply for the loan. Origination fees can take a number of forms: a flat dollar amount, a percentage of the loan amount (*i.e.*, an "origination point"), or a combination of the two. Origination points or fees may also be framed as a single lump sum or as several different fees (*e.g.*, application fee, underwriting fee, document preparation fee).

1129 20TH STREET, N.W. • NINTH FLOOR • WASHINGTON, DC • 20036 •
WWW.CSBS.ORG • 202-296-2840 • FAX 202-296-1928

Because these types of pricing structures are present in the vast majority of originations and the payment of upfront points and fees is widespread, the CFPB has estimated that implementation of the Dodd-Frank requirement without adjustment would cause the industry to face radical restructuring of its existing price structures and practices. The CFPB is thus proposing to use its exception authority under Dodd-Frank to allow creditors to continue making available loans with points and/or fees, so long as they also make available a comparable, alternative loan. The alternative loan would be a "zero-zero" loan, meaning it would include no upfront discount points, origination points, or origination fees that are retained by the creditor, broker, or an affiliate of either.

CSBS concurs with the CFPB's analysis regarding the detrimental impact a flat ban on upfront points and fees would have on the mortgage industry. Additionally, we believe the CFPB is correct in maintaining the proposed alternative will make it easier for consumers to evaluate different pricing options, while preserving their ability to make some upfront payments if they want to reduce their periodic payments over time. We therefore support CFPB's proposed exception to the Dodd-Frank requirement as a means for promoting stability in the mortgage market, while benefiting both consumers and creditors.

Critical to the success of the zero-zero alternative framework is a standard whereby the difference between the higher interest rate on the no-fee loan and the interest rate on the loan with upfront fees must be reasonably related to the amount of upfront fees. This standard must be properly enforced to prevent unreasonably larger margins in secondary market pricing that allow a large enough credit to cover closing costs and result in further compensation for creditors. Additionally, in response to a CFPB inquiry, CSBS strongly supports the adoption of a "bona fide" requirement to ensure that consumers receive value in return for paying upfront points and/or fees.

RESTRICTIONS ON LOAN ORIGINATOR COMPENSATION

Interpretation of existing LO Compensation standards can be difficult for regulators and consumers. The CFPB is proposing measures to adjust current rules governing compensation to loan officers and mortgage brokers in connection with closed-end mortgage transactions to provide greater clarity and flexibility where needed. CSBS believes adjustments to existing rules for purposes of clarity and coherence are appropriate.

Specifically, the CFPB has proposed to continue the general ban on paying or receiving commissions or other loan originator compensation based on the terms of the transaction (other than loan amount), with some important refinements. Above all, the proposal would allow reductions in loan originator compensation to cover unanticipated increases in closing costs from nonaffiliated third parties under certain circumstances. The current Loan Originator Compensation Rule does not allow creditors and brokerages to set a loan originator's compensation at a certain level and then lower it in selective cases where different loan terms are negotiated because such a structure could be used to circumvent the ban on compensation based on a transaction's terms or conditions. CSBS supports the CFPB's inclination to allow concessions when made in response to unforeseen events genuinely outside the loan originator's control. Such concessions should not raise concerns about the potential for steering consumers to different loan terms. The provisions outlined the CFPB will provide needed clarity in this area.

Additionally, under the Loan Originator Rule, compensation based on a factor that is a proxy for a transaction's terms or conditions is prohibited because compensation based on proxies could potentially lead to circumvention of the ban on compensation based on the terms and conditions of the loan. Credit scores and debt-to-income ratios are examples of factors that are proxies for loan terms. CSBS endorses the CFPB's efforts in clarifying when a factor used as a basis for compensation is prohibited as a proxy for a transaction term. We encourage the CFPB to issue a more precise definition of the term "proxy," however, since no definition is provided in the proposal.

Another critical clarification addressed in the proposal surrounds point bank programs. Under the Loan Originator Rule, a point bank could be viewed as compensation since it is providing "a financial or similar incentive" to an originator. In a point bank, a creditor contributes points to an LO for each transaction that the LO closes. The LO may then use these points to obtain pricing concessions from the creditor. For example, the LO may pay discount points to the creditor from the LO's point bank in order to obtain a lower rate for the consumer. Point banks may exist in both retail and wholesale contexts. Stakeholders have wondered within the context of the Loan Originator Rule whether there are any circumstances under which point banks are permissible. CSBS supports the CFPB's clarification that there are no circumstances under which point banks are permissible. We support the continued prohibition on point banks, as such systems represent impermissible concessions in LO compensation structures.

The proposal would also clarify and revise restrictions on pooled compensation, profit-sharing, and bonus plans for originators, depending on the potential incentives to steer consumers to different transaction terms. Above all, the proposal would permit employers to make contributions from general profits derived from mortgage activity to 401(k) plans, employee stock plans, and other "qualified plans" under tax and employment law. CSBS believes this is one of the primary areas under the Loan Originator Rule that needs clarification, and we endorse the CFPB's proposal to permit contributions to qualified plans.

Further, the proposal would permit employers to pay bonuses or make contributions to non-qualified profit sharing or retirement plans from general profits if either: (1) the loan originator affected has originated five or fewer mortgage transactions during the last twelve months; or

(2) the company's mortgage business revenues are limited. Importantly, even though contributions and bonuses could be funded from general mortgage profits, the amounts of such contributions and bonuses could not be based on the terms of the transactions that the individual had originated. CSBS believes the CFPB's adjustments in the area of non-qualified programs are largely appropriate. However, we note that enforcing standards based on thresholds for origination, such as the "five or fewer" measurement contained in this proposal, can be problematic, as the number of mortgage transactions originated may have differing degrees of significance in different scenarios. We encourage the CFPB to either justify the level through study or adopt a more flexible approach that can be tailored to various situations appropriately.

OTHER

The CFPB has proposed to implement other Dodd-Frank requirements applicable to both closed-end and open-end mortgage credit. First, the proposal would ban general agreements requiring consumers to submit any disputes that may arise to mandatory arbitration rather than filing in court. CSBS endorses this provision as a positive measure for consumers. With binding mandatory arbitration, consumers are often required to agree to waive their right to sue, to participate in a class action lawsuit, or to appeal. Consumers may be unaware that they have agreed to binding arbitration or of the legal consequences of such a provision. Also, consumers may need to pay a significant fee to initiate arbitration and participate in arbitration, including paying all or a portion of the arbitrator's hourly fees. These expenses may be more than if the consumer were to file a lawsuit. Such provisions would likely be presented on a "take it or leave it" basis, which would be unfavorable to consumers. Lastly, mandatory arbitration generally binds the consumer but may not bind the business.

The proposal would also generally ban the financing of premiums for credit insurance. We support the general ban on financing of premiums for credit insurance, as premiums are often financed for a longer period than the coverage of the insurance.

Thank you for the opportunity to comment. We appreciate the CFPB's work in clarifying these standards.

Sincerely,

John W. Ryan
President and CEO