

Regarding the proposed draft one page disclosure form mandated by HB 2770

1. A fundamental problem that exists within the mortgage broker industry is the refusal of mortgage brokers to tell their customers what they will earn for providing origination services. As a result, the consumer has been unable to draw a relationship between the services provided and the total cost to the consumer for that service. SB 6381 puts an end to this evasion. Until now, the question of compensation has been open ended and its dollar amount poorly disclosed. That together with substantial conflicts of interest inherent in the YSP based compensation model has contributed much to the current problems. This changes with the passage of SB 6381. As fiduciaries, brokers must, at the very least, state in simple terms their compensation for providing mortgage loan origination services. The proposed disclosure form is inconsistent with that fiduciary responsibility. Language such as "you may be charged these fees" when referring to origination and/or broker fees is inadequate. The broker or his LO must state what they are going to charge (their total compensation) for origination services in plain language. It is also inconsistent with that fiduciary responsibility to split the broker compensation up into segments (origination fee, processing fee, broker fee, etc) – that strategy serves only to obfuscate the actual cost to the borrower and as such does not serve the borrower's best interest.

2. Under 'SPECIAL FACTORS YOU MUST BE AWARE OF' there is a check box line that says the "mortgage broker will receive a yield spread premium of \$___". YSP and Discount points are terms referring to the opposite ends of the pricing continuum offered by the lender. Neither is known absolutely until after the loan is locked. What is not clear (and HB 2770 is all about clarity) is what happens if the YSP increases after this disclosure is made? What happens if it decreases? In the interest of clarity this needs to be explained. In the interest of clarity and to be consistent with fiduciary responsibility, the only acceptable disclosure regarding YSP is a statement that any YSP will be credited to the borrower against closing costs. This adds clarity and removed conflicts of interest as is required by the application of fiduciary responsibility.

3. Under the disclosure of "YOU MAY BE CHARGED THESE FEES": The form calls for the disclosure of Discount Points. HB 2770 calls for the elimination of "misstatements and misrepresentations". In the "true" brokered transaction there is no such thing as a fee called "discount points". One of the many myths created by the mortgage broker industry is that borrowers must pay a fee by the name of "discount points" to obtain a lower interest rate. I have been working with lender ratesheets for 13 years and I have never seen a fee called "discount points" listed as a fee that lenders charge. It has been, is, and will be a misstatement for a broker to claim that the lender charges such a non-existent fee. For loans originated at an interest rate below the par rate the lender pays a discounted price. The resulting deficit is made up by the borrower. Through the years this deficit which results from the discount price the lender is paying has come to be known as discount points. But it is not a fee! And it is a misstatement and a misrepresentation to refer to it as a fee.

4. Under 'SPECIAL FACTORS YOU MUST BE AWARE OF' there is a check box line providing disclosure of pre-payment penalties if they exist. In many loan programs, pre-payment penalties are an option that can be added to the loan. The result is an increase in the price the lender will pay relative to the same loan without the pre-payment penalty. When the loan interest rate is above par, this means that there is more YSP as a result of the pre-payment penalty. If the broker is selecting the pre-payment penalty with the

intent of creating more YSP which will be claimed as compensation, then the selection of the penalty creates a conflict of interest. SB 6381 requires brokers to act as fiduciaries. This means that they must eliminate, as far as practicable, all conflicts of interest, and at the very least fully disclose conflicts that exist. So the simple disclosure of a pre-payment penalty is inadequate. The fiduciary owes it to his borrower to state that the penalty is an option (if it is) and that the selection of the penalty has an impact on the price that the lender will pay for the loan. It either increases the broker's compensation or it decreases the borrower's closing costs. While the disclosure of the pre-payment penalty is important, it is also important that the borrower be made aware of the fact that it is an optional choice (if it is) and of the consequences of making that choice and of any conflicts of interest the broker may have in recommending the selection of the penalty.

5. Under 'SPECIAL FACTORS YOU MUST BE AWARE OF' there is a check box line that says a "cost was charged to you because your loan is based on reduced documentation of income and assets". Once again, we are creating a misstatement and misrepresentation; HB 2770 specifically prohibits misstatements and misrepresentations. Lenders do not charge a fee for reduced documentation. They adjust the price that they will pay. While this may sound like semantics, it is an important distinction. It is a misrepresentation and a misstatement to suggest that anyone is charging fees where no such fees are charged. In the interest of clarity, it is important that borrowers learn and understand that in the brokered transaction, the key term is the price that the lender may pay for a given loan. That is the fact of the matter, and any description to the contrary is a misstatement and is not allowed by HB 2770.

6. Is it the intent of the department that this form be reissued when any of the "material terms" listed change? Lender pricing changes at least daily and often several times during the day. Disclosed terms such as discount points and YSP are derivatives of the lender's price and so they change at least daily until the loan is locked. Is it the intent that this form be reissued at every change?

7. Would it not make sense to draft this disclosure form with both HB 2770 and SB 6381 in mind? This proposed draft does not consider the implications of SB 6381. It appears that we will have to revise it in light of SB 6381. Would it not make sense to get it right with both of these new laws in the first place?

8. HB 2770 requires the department to adopt by rule a one page disclosure summary form that provides "*plain language terms that are reasonably understandable to the average person without the aid of third party resources*". The clear intent is to provide clarity to the myriad disclosures that already exist in the typical loan package. This proposed draft disclosure form fails to achieve this mandated purpose. All it does is consolidate the disclosures that already exist. It does nothing to make them plain and understandable to the average person. For example, yield spread premium is not a term that the average person understands. Indeed, it is not a term that many loan originators understand. Even the Federal Reserve Board got it wrong in a recently promulgated draft change to TILA. So stating that the broker "will receive a yield spread premium of \$____" doesn't add any clarity beyond that which is already poorly provided in the good faith estimate and one cannot conclude that the average person can understand the disclosure the meaning and significance of this disclosure.

9. I propose the following as a more clear plain language disclosure summary:

You are engaging (firm name) for mortgage loan origination services. We have determined that our fee for originating your loan will be \$_____. This fee will be included as a part of the total closing costs in addition to other fees as disclosed on the good faith estimate. We will receive no other compensation from any other source in conjunction with this loan. This fee (is/is not) subject to change. (Please refer to our contract for the conditions under which the fee might change.)

We will submit your loan application to one of the lenders we work with. It is important you understand that, if approved, a lender will purchase your "note" and that the price to be paid depends on several factors one of the most significant of which is the interest rate you select. The lender offers prices across a wide range of interest rates. You may select a rate at the lower end of the range for which the lender will purchase your note at a price that is less than the loan amount. In such a case you may need to make up the difference between the loan amount and the price to be paid. This difference is commonly referred to as 'discount points'. Alternatively, you may select a rate at the higher end of the range. At higher interest rates the lender offers to pay a price that exceeds the loan amount. You might choose a higher interest rate loan to produce such an excess to help pay some or all of your closing costs.

You may choose to pay closing costs (including our fee) by any or a combination of the following:

(a) You may select a loan amount and interest rate such that you pay some or all of your closing costs, including our fee, out of pocket. (b) You may, in some cases, be able to increase your loan amount and use the excess borrowed funds to pay some or all of your closing costs. (c) You may choose a higher interest rate such that the lender pays you more for your note than the loan amount and use the excess price received to pay some or all of your closing costs.

You are applying for (or contemplating) a loan for the amount of \$_____ at an interest rate of _____%* For this loan amount (note amount) and interest rate and the program you have agreed to and based on one lender's prices in effect today, and assuming your loan is approved, the following apply:

The lender will pay \$_____** for your note. At this price (which will change at least daily until you lock the loan) you will need to pay discount points of \$_____ in addition to other closing costs OR you will receive \$_____ from the lender to apply toward your closing costs. A table showing how this price compares at higher and lower interest rates is attached.

You may elect to attach a pre-payment penalty to your loan. If you elect a pre-payment penalty, the price the lender will pay will be increased by \$_____. I (do/do not) select a pre-payment penalty. The terms of the penalty are shown on the attached page.

You may elect an interest-only payment schedule. If you elect this schedule, the lender will decrease the price to be paid by \$_____. I (do/do not) select the interest-only option. The terms of the interest only option are shown on the attached page.

You may choose to provide less than complete documentation of your income and assets to be considered by the lender. If you choose a low or no documentation loan, the lender price will be reduced by \$_____. I (do/do not) select a low documentation loan program.

You may elect to have your property taxes and home owner's insurance included in your mortgage payment. If you choose to have the lender collect property tax and HO insurance in your mortgage payment, the lender will increase the price to be paid for your loan by \$_____. I (do/do not) desire my property taxes and home owners insurance to be included in my mortgage payment.

*The terms of the loan you are applying for (or are contemplating) are as follows:

This loan interest rate is fixed for the life of the loan. The term of this loan is _____
 This loan is an adjustable rate loan. The interest rate starts at ____%. This rate will remain in effect for _____ months. After this time the interest rate and your payment can go higher on _____ and each _____ month(s) after that. Today's estimate of how high the interest rate can go, called the fully indexed rate, is ____%. The maximum possible interest rate on your loan is ____%. Your maximum monthly payment could be \$_____. You should review these terms as detailed in your note to be sure that you understand them. A sample copy of the note for this loan program is provided.

** This price is based on a lock period of _____ days.