

Restoring Faith to Rebuild the Industry

To earn consumer confidence, legislation and mortgage-industry professionals should promote education

By **Tom Heath**, owner, Rio Nuevo Financial LLC

WITH ALL THE LEGISLATION proposed and passed in recent months, the mortgage industry is going through a metamorphosis. Amid the fear and uncertainty that have ruled the real estate and financial markets for the past two years, legislatures reacted to a crisis of epic proportions, and regulators tried to keep a struggling economy moving, albeit with conflicting messages.

Despite the differing messages, much of the reform process has a common theme: protect consumers and restore faith in the industry. To do this, however, it is essential that legislation and regulation promote consumer education.

Education, along with better-coordinated efforts to rebuild the industry, can help restore consumers' faith in the industry.

Solutions: A timeline

Federal regulators have tried to find a solution to the housing and mortgage market crisis. There has not been a cohesive plan to rebuild this industry, however. Rather, there has been a series of related — but not connected — regulatory proposals and rules.

Here's a look at some of the key regulatory events of the past few months, as they relate to the mortgage industry:

- **March 14:** The U.S. Department of Housing and Urban Development (HUD) releases a 96-page proposal to reform the Real Estate Settlement Procedures Act (RESPA). Part of the proposal includes replacing the current one-page good-faith estimate with a four-page version. According to HUD, it is necessary to disclose a mortgage broker's yield spread premium (YSP) to give consumers clarity on originators' profits.
- **July 14:** The Federal Reserve announces rules

to amend Regulation Z, which implements the Truth in Lending Act. Among the changes, stated-income loans and prepayment penalties are eliminated for nonprime borrowers. Also, high-cost lending is redefined. The Fed, however, preserved YSPs in their existing form, retracting its earlier efforts to eliminate them.

- **July 30:** The Housing and Economic Recovery Act of 2008 establishes the framework for housing- and mortgage-market recovery. The bill provides a multifaceted approach to reduce foreclosures and spur home sales. It also prohibits its seller-financed downpayments and issues a

moratorium on HUD's higher, risk-based insurance premiums for FHA-insured loans.

- **July 31:** House Resolution No. 6694, the FHA (Federal Housing Administration) Seller-Financed Downpayment Reform and Risk-Based Pricing Authorization Act of 2008, is introduced. If passed, the bill would revise the requirements for seller-financed downpayments for mortgages for single-family housing insured by the HUD secretary under Title II of the National Housing Act and would authorize risk-based insurance premiums for certain mortgagors under such mortgages.
- **Aug. 11:** Concerned that proposed RESPA reform would be duplicative and inconsistent with the Fed's recent changes, 240 members of Congress join other federal agencies to urge

HUD to withdraw its current RESPA-reform efforts. They argue that HUD's suggested, revised four-page good-faith estimate does not provide borrowers with the necessary clarity in the transaction. They ask HUD to wait until a comprehensive study can be done to ensure consumers are provided with a transparent loan process.

- **Sept. 7:** Fannie Mae and Freddie Mac are placed under government conservatorship.
- **Sept. 28:** After a series of bank failures and government interventions, Congress members indicate that passing a \$700 billion bailout pack-

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age designed to buy toxic mortgages and restore liquidity in the market is imminent.

- **Sept. 29:** U.S. House of Representatives rejects first stab at rescue plan for the financial industry, and the stock market plunges.
- **Oct. 1:** The Senate passes a bailout bill similar to the one that failed in the House days earlier.
- **Oct. 3:** The House passes the Senate's version of the bill, and the president signs the legislation into law.

Signs of stability?

In early September, Global Insight, a privately held forecasting company, announced that although house prices were still falling nationwide, there was not extreme overvaluation of prices, indicating that the housing bubble has popped.

Then on Sept. 7, U.S. Department of the Treasury Secretary Henry Paulson announced that Fannie Mae and Freddie Mac would be placed under conservatorship under the control of the newly created Federal Housing Finance Agency. A conservatorship allows the government to

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Restoring Faith

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step in, provide stability, restructure the organizations and possibly return them to private control. Treasury officials previously compared the process to Chapter 11 bankruptcy.

Fannie Mae's and Freddie Mac's conservatorship could ultimately cost taxpayers billions of dollars because it requires the government to cover the debt and delinquent loans held by the two GSEs. Paulson countered this concern, saying, "Fannie Mae and Freddie Mac are so large and so interwoven in our financial system that a failure of either of them would cause great turmoil in our financial markets here at home and around the globe."

Some contend, barring any unexpected

for loan originators and reinforces efforts to ensure individual states license their originators. Licensing and education are keys to creating professional originators. It has been too easy to originate loans without having the proper training and the necessary accountability. The national database is expected to minimize the ability of bad originators to resurface in other states. With continuing-education requirements, mortgage brokers will be held to a higher standard than before.

Further, it is a basic tenet of the U.S. capitalistic market that lenders should be able charge more for their products and maximize their profits. Likewise, with choices, consumers can compare loan programs, rates, fees, service and reputation to decide on which lender to use.

The debate about the role of YSPs has just

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upheaval, that housing prices have stabilized and that the government takeover of Fannie and Freddie, as well as the \$700-billion bailout plan, will help to stabilize the credit markets. They say that this could lead to the development of the foundation on which we can rebuild our housing and credit markets.

The cornerstone of reconstruction

Certainly, the government must protect consumers. But it must do while maintaining fiscal responsibility and promoting a robust economy.

Legislation, however, does not guarantee good behavior. Rather, it often punishes bad behavior. Those who defrauded the system or misled their customers did so despite current regulation. Increased regulation likely will not alter their motives.

This past July's Housing and Economic Recovery Act of 2008 creates a national registry

begun, but we do a disservice to consumers if we direct their attention to the lender's or broker's profit and away from the cost of their loan.

The cornerstone of the reconstruction, therefore, must be consumer education. To restore faith in the mortgage industry, it is critical that consumers become more educated about the loan process. The government will act to protect consumers, but that protection should not result in eliminating products or choices. Simply having a loan with the lowest rate or the lowest cost is not always the best option for the consumer.

As with any product purchase, there is a price and a value associated with a mortgage. And as with any investment, there also is risk.

Brokers, bankers, legislatures and consumers must work together to create a system that produces educated and informed borrowers who can evaluate the cost, the value and the risk. **■**