



February 2, 2022

CFPB Regulation of Smaller IMBs

The Honorable Rohit Chopra
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Dear Director Copra:

The Community Home Lenders Association (CHLA)¹ writes: (1) to inquire what policies and actions the CFPB has taken regarding the Dodd-Frank statutory requirement for *tiered supervision of independent mortgage banks (IMBs) based on size, volume, and extent of state supervision*, and (2) to express our *strong opposition to any use of “regulation by enforcement,”* particularly for smaller IMBs.

The Dodd-Frank “*Wall Street Reform and Consumer Protection Act*” requires CFPB regulatory tiering for smaller IMBs. Specifically, Subsection 1024(b)(2) of the Dodd-Frank legislation, which deals with CFPB regulation of non-bank financial services firms, requires the following (our bolding):

“(2) **RISK-BASED SUPERVISION PROGRAM. The Bureau shall exercise its authority under paragraph (1) in a manner designed to ensure that such exercise, with respect to persons described in subsection (a)(1), is based on the assessment by the Bureau of the risks posed to consumers in the relevant product markets and geographic markets, and taking into consideration, as applicable—**

- (A) the asset size of the covered person;**
- (B) the volume of transactions involving consumer financial products or services in which the covered person engages;**
- (C) the risks to consumers created by the provision of such consumer financial products or services;**
- (D) the extent to which such institutions are subject to oversight by State authorities for consumer protection;**
- (E) any other factors that the Bureau determines to be relevant to a class of covered persons.”**

CHLA appreciates the important role that the CFPB plays in ensuring consumer confidence in our mortgage markets, and in preventing outlier firms from engaging in practices which harm consumers and create an unfair competitive advantage relative to compliant firms. However, as this letter explains, smaller IMBs do not have the economies of scale that larger IMBs have to extensively monitor how the CFPB might deviate from state interpretations of the large array of federal consumer mortgage rules and regulations.

Moreover, CFPB adherence to the tiered supervision requirements serves three pro-consumer purposes. It:

- 1. Maximizes the effectiveness of the deployment of CFPB resources to protect consumers.**
- 2. Reduces lender concentration, thus increasing competition and reducing mortgage rates & fees.**
- 3. Reduces costs for community lenders, that provide more personalized service to borrowers.**

¹ CHLA is the only national trade association that exclusively represents independent mortgage bankers (IMBs). Our members are small and mid-sized IMBs whose sole business is originating and servicing mortgage loans. [[See communitylender.org](http://Seecommunitylender.org)].

The Importance of Tiered Supervision of IMBs

Every IMB is subject to supervision and enforcement actions of both federal and state consumer protection laws by its primary regulator(s) – i.e. every state in which an IMB originates or services mortgage loans. In addition, every IMB - no matter how small or how few loans it originates - is subject to duplicative supervision and enforcement by the CFPB with respect to these same federal consumer protection laws.

Such dual regulation leads to cost burdens that disproportionately affect smaller IMBs, which lack the compliance economies of scale of larger IMBs. It is not uncommon for smaller IMBs to spend hundreds of thousands or millions of dollars – not out of concern that the IMB is not compliant with federal mortgage rules and regulations – but because of the risk the CFPB may have a different interpretation of the firm’s compliance with the rules than their state regulators. Additionally, smaller IMBs may expend resources to be fully prepared for a CFPB exam (which may never come) that may differ from their state exams.

Larger IMBs can spread such costs over a much larger loan base. Smaller IMBs cannot. Several years ago, CHLA submitted to the CFPB a detailed cost estimate by one of our members of incremental costs related to preparation for CFPB exams and rule interpretations – translating these costs into the added cost per loan for that firm, and showing it would have had a much more significant cost impact for an even smaller firm.

Thus, smaller IMBs are faced with a choice: (1) incur significant CFPB exam preparation and monitoring costs that, spread over a small loan volume base, make them less competitive, or (2) risk significant CFPB penalties if the CFPB disagrees with an IMB’s good faith effort to comply with rules and regulations.

The majority of small IMBs are closely held firms, where the principal owner(s) has skin in the game. For such firms, the risk of significant CFPB fines has a personal impact, unlike banks and publicly held IMBs, where shareholders bear the risk. Whichever option an IMB pursues from the prior paragraph, this is yet another factor that contributes to increasing consolidation of the IMB mortgage industry or to IMBs going public in order to grow. Industry consolidation reduces competition and thereby hurts consumers.

We assume that it was for these types of reasons that Dodd-Frank exempted 97% of banks (those under \$10 billion in assets) from CFPB supervision and enforcement. In lieu of providing an explicit exemption from CFPB supervision for smaller IMBs, Dodd-Frank included the tiered regulation language cited above.

CHLA appreciates that the CFPB appears to focus both its exams and enforcement actions more on larger IMBs, consistent with the statute. However, this provision is of limited value to smaller IMBs, if an IMB can be subject to CFPB exams and significant enforcement penalties with little or no notice, even when, for the great number firms, they are acting in good faith to fully comply with all mortgage rules and regulations.

Without any clarification about how CFPB is implementing the tiering requirement, smaller IMBs will be forced to continue to spend significant amounts of funds – to no consumer or economic benefit – to hire staff, lawyers, and outside consultants to closely track CFPB interpretations of a large array of federal rules.

Therefore, CHLA is asking what steps the CFPB is taking to comply with the Dodd-Frank risk-based tiered supervision requirements.

CHLA also requests that the CFPB adopt a public statement or formal policy that it will exempt smaller IMBs from being subject to CFPB exams or audits – ideally listing an annual loan origination cutoff dollar or loan amount and a servicing cutoff dollar or loan amount.

CHLA also requests that CFPB adopt a policy that it will not initiate enforcement actions against smaller IMBs unless requested to do so by one of the IMB’s state regulators. This strikes a balance between unnecessary redundant regulation and maintaining CFPB’s authority to take action when it is merited.

Why Regulation by Enforcement is a Significant Problem for Smaller IMBs

Our concerns cited in the previous section could be significantly mitigated by a public statement or formal policy that the CFPB will not use “*regulation by enforcement*” against smaller IMBs. By that, we mean that the CFPB should not impose fines or penalties against smaller IMBs for compliance actions that are taken in a good faith effort to be in compliance with a particular mortgage rule or requirement.

The CFPB has at times imposed significant fines for prior behavior, without first giving a firm the opportunity to correct compliance issues or problems the CFPB identifies. As noted in the prior section, significant CFPB fines have a particularly significant impact on the owners of smaller IMBs, as it is usually individuals that personally pay the fines, unlike banks or publicly held firms, where shareholders do.

CHLA believes that the primary goal of regulation should be to foster compliance by all market participants, and not to generate fines for the sake of generating fines.

Therefore, CHLA recommends that the CFPB adopt a formal policy of allowing a smaller IMB the opportunity to correct a violation identified by the CFPB prior to the CFPB imposing fines or taking enforcement action – providing the IMB was making a good faith effort to comply with a rule. Of course, fines and enforcement actions are appropriate after such point if the IMB does not correct.

We understand that the threat of fines for actions before the CFPB identifies an individual firm’s actions as problematic can have a deterrent effect on bad behavior. We also appreciate that some consumers may be impacted prior to the CFPB notifying a smaller IMB of noncompliance.

However, the consumer impact is limited for smaller IMBs, since they serve significantly fewer consumers than large mortgage lenders. A requirement that an IMB acted in good faith to comply with the rules – as opposed to actions with the intent to harm customers – also significantly limits the consumer impact. Finally, this treatment is also consistent with the statutory tiering requirement.

Thus, the CFPB should first give smaller IMBs a chance to correct compliance issues before imposing fines.

Such an approach would mirror that of other financial regulators such as the FDIC, which uses memorandums of understanding (MOU), a common informal agreement used to obtain a commitment from a bank’s board of directors to implement corrective measures. Other informal actions that the CFPB could consider include board resolutions, letter agreements, and other forms of bilateral agreements or actions.

Maximal CFPB Guidance on Rules and Regulations Enhances Compliance

Finally, with the objective of enhancing compliance, CHLA recommends that the CFPB make it a priority to provide timely and explicit guidance to IMBs on mortgage compliance rules. Our suggestions are:

- The CFPB should make it a priority to provide maximal guidance on all mortgage rules and regulations.
- The CFPB should provide timely detailed responses to all compliance questions submitted by IMBs.
- A safe harbor from enforcement action should be provided when a firm complies in good faith with CFPB guidance or a CFPB response to a specific compliance question (or fails to respond to such request).

Thank you for consideration of these comments and requests.

Sincerely Yours,

COMMUNITY HOME LENDERS ASSOCIATION