May 1, 2023

Regulation Z Mortgage Loan Originator Rules
Docket No. CFPB-2023-0017

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

Dear Director Chopra:

The Community Home Lenders of America (CHLA)[1] writes to provide comments in response to this request for public comment regarding the Bureau's Loan Originator Compensation ("LO Comp") rule.

The purpose of this comment letter is to request targeted flexibility with regard to LO Comp restrictions, in order to benefit consumers without opening up loopholes that would facilitate steering or other anti-consumer practices that are at the heart of the LO Comp rule.

The LO Comp statutory provision and the rule implementing it generally prohibit LO compensation from varying based on the terms of the loan (other than the principal amount of the mortgage loan). However, the inflexibility of the rule in a few areas actually works to the detriment of consumers. Therefore, CHLA writes to ask for flexibility from the strict prohibition against variations in LO compensation in the following three situations:

1. **State HFA Bond Loans.**
2. **Truly competitive situations, in order to enable a lender to match a price offer.**
3. **Loan originator Error.**

<u>Authority to Reduce Compensation on Housing Finance Authority (HFA) Loans</u>

State Housing Finance Agencies (HFAs) operate bond programs to facilitate low down payment single family homeownership programs to help qualified families become first time homebuyers.

However, such bond programs typically involve more complexity than other single family loan options, including robust underwriting, tax law-related paperwork, yield restrictions, limits on rates and fees, and other program requirements. As a result, HFA loans are generally more expensive to manufacture.

Before the LO Comp rule, it was common for the lender to absorb some of these costs by paying their loan originators a smaller fee for an HFA loan than a non-HFA loan. The LO Comp rule put an end to that.

The inability to reduce loan originator compensation to offset HFA production costs under the current LO Comp rule harms consumers by discouraging lender participation in these vital programs. Moreover, because HFA loans are generally more costly to underwrite and therefore less profitable, providing LO comp flexibility for such loans does not create financial incentives to steer borrowers to higher priced loans.

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[1] CHLA is the only national trade association focused exclusively on small and mid-sized independent mortgage banks (IMBs).

Allowing an exception for state bond loans would still not permit compensation to vary based on the terms of a loan - but instead only on whether a loan is or is not an HFA loan. The prohibition against varying compensation among all of an individual lender's HFA loans could still be retained.

Finally, creating flexibility for this category of HFA loans is a simple bright line test.

Authority to Reduce Compensation in Order to Match a Competitor's Offer for a Consumer that the Loan Originator Has Been Assisting

The Bureau has encouraged mortgage loan competition and consumer price shopping. However, an overly restrictive limitation that compensation may not vary can interfere with that objective.

Lenders are currently permitted to respond to a consumer that is price shopping by lowering the rate to match a competing loan offer. However, the prohibition against reducing (varying) LO compensation discourages such actions, since a lenders' profit would be reduced or eliminated without the commensurate ability to reduce compensation being paid to LOs.

The impact is to reduce a lender's willingness to engage in such a competitive price matching. Many lender groups have for some time argued for targeted flexibility for loan originators in this situation, typically asking for such flexibility when there is ***"demonstrable price competition."***

CHLA is sympathetic to a position that this standard of "demonstrable price competition" should be narrow, in order to maintain the underlying objectives of the LO Comp rule.

Following is a proposal that addresses these concerns, by identifying objective and targeted circumstances necessary to meet a standard of demonstrable price competition and prevent a lender from using this flexibility routinely to adjust rates and terms based on different types of borrowers. Specifically, CHLA recommends the following conditions should be established to use LO Comp pricing flexibility:

1. *The lender has an agreed upon a compensation schedule for the loan originator and has provided a loan estimate, with specific rates and terms, to a potential borrower.*

2. *The lender has provided substantial assistance to the borrower over some time period - e.g., helping the borrower qualify for a loan, helping the borrower identify the best loan option, etc. - and the borrower then asks the lender to match a better offer from a different lender.*

3. *In response to this request, the lender matches the offer from the other lender.*

4. *The lender does not make regular use of this flexibility [note: the CFPB could set some general standard or percentage cap to prevent its indiscriminate use].*

5. *The lender must maintain a log or in some other way provide documentation that it has met all of the four preceding requirements.*

CHLA can provide representative examples of this set of circumstances. We cite an actual case from one of our members, where a loan originator assisted a borrower over the course of four months to pre-qualify and help the consumer make purchase offers on several homes. On the fourth such offer, the consumer entered into escrow on a home and completed a loan application and the lender provided a loan estimate.

Using the right to shop, the consumer then obtained a loan estimate from a different lender, with a lower rate. Without the lender's ability to reduce compensation to the LO, the lender's profit would have been eliminated by matching the competing offer, so the lender did not do so. Therefore, the loan originator lost the loan and the consumer as a client - even though the loan originator was willing to accept reduced compensation in order to close the loan and maintain a long-term relationship with the consumer.

This outcome is unfair to the consumer who wants to consummate the loan with the original lender, but cannot justify the inferior terms. This outcome is also unfair to the lender and its loan originator that spend time assisting the borrower with the loan process, but end up losing the loan. To make matters worse, the consumer may end up with a negative impression of the lender's failure to match the terms, as a borrower may understandably be skeptical about the explanation that Bureau rules make matching the offer more difficult.

Our proposal provides an objective standard for *"demonstrable price competition"* and ensures that cost savings achieved by reducing compensation are passed along to the consumer. It does not result in variations in compensation based on loan terms, but instead on the targeted and limited circumstances that meet the price matching criteria we are suggesting.

Authority to Reduce Compensation When a Loan Originator Makes an Error

Finally, the Bureau should permit the customary compensation a loan originator receives from its lender employer to be reduced by the costs associated with an error made by that same loan originator.

This is based on the simple principle that loan originators should take financial responsibility for their errors.

This is a simple bright line test that does not involve compensation varying based on the terms of the loan. Lenders should be given guidance to ensure accountability via documented policy and procedure. If a lender reduces compensation due to error, the lender should be required to document the incident and maintain a log of such incidents – and track all corrective action including but not limited to the originator entering training programs to ensure repeat offenses do not occur.

There is only a benefit, no downside, to the consumer. Moreover, it is only fair that the loan originator, not the lender, should absorb such costs. Allowing this change also facilitates financial accountability on the part of the loan originator, which should result in fewer loan errors, which in turn will reduce a lender's operational costs, which can be passed along to the consumer.

In order to exercise this flexibility, the lender should be required to document:

- The error made in every instance in which compensation is reduced,
- The Loan Originator received training and guidance before the error was made.
- This is not just one transaction, but represents more than one error by the same Loan Originator.

Thank you for consideration of these recommendations.

Sincerely,

COMMUNITY HOME LENDERS OF AMERICA