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# EXAMINING REGULATORY BURDENS ON NON-DEPOSITORY FINANCIAL INSTITUTIONS

## HEARING

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTEENTH CONGRESS

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# EXAMINING REGULATORY BURDENS ON NON-DEPOSITORY FINANCIAL INSTITUTIONS

**Wednesday, April 15, 2015**

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER CREDIT,
COMMITTEE ON FINANCIAL SERVICES,
*Washington, D.C.*

The subcommittee met, pursuant to notice, at 1:01 p.m., in room 2175, Rayburn House Office Building, Hon. Randy Neugebauer [chairman of the subcommittee] presiding.

Members present: Representatives Neugebauer, Pearce, Lucas, Posey, Fitzpatrick, Luetkemeyer, Stutzman, Mulvaney, Pittenger, Barr, Rothfus, Dold, Guinta, Tipton, Williams, Love; Clay, Scott, Maloney, Sherman, Lynch, Delaney, Heck, Sinema, and Vargas.

Ex officio present: Representative Waters.

Chairman NEUGEBAUER. The Subcommittee on Financial Institutions and Consumer Credit will come to order. The Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "Examining Regulatory Burdens on Non-Depository Financial Institutions."

Before I begin, I would like to thank our witnesses for being here today, and for traveling all the way over here to room 2175. As you know, our regular committee room is under construction for a little remodeling, making sure that it is ADA-compliant, and upgrading the sound system so that when the Federal Reserve Chair is here, we don't have to adjourn for 10 minutes while we try to get the sound back on.

And so, we are very happy that you are here today. This is a very important hearing, and I look forward to hearing from our witnesses this afternoon.

At this time, I will recognize myself for 5 minutes for an opening statement.

Good afternoon. This month, we got some very bad economic news: The U.S. economy only created 126,000 jobs in the month of March, far below our expectations. The Government also revised the numbers downward for the first quarter.

I see these numbers, and I continue to be concerned with the direction that our economy is headed. According to the Brookings Institute, last year, for the first time in 30 years, business deaths exceeded business births.

And on this day, tax day, we are reminded just how burdensome and complex our Tax Code is; according to the National Taxpayers Union Foundation, compliance with Federal income tax cost the economy $233 billion in productivity last year. This is only making it harder to get our economy back on track.

This committee has already heard testimony on and explored the significant regulatory onslaught and resulting market consolidation facing our depository institutions, our Nation's community banks and credit unions.

Today, I am pleased to welcome our witnesses, who represent many small businesses and community-based financial institutions, to hear their perspective on ever-increasing regulatory burdens.

As many of you know, the full Financial Services Committee and this subcommittee are undertaking a comprehensive examination of regulatory burdens facing our Main Street lenders and businesses. Today's hearing provides the committee with an opportunity to hear about the impact that these regulatory burdens have on our non-depository financial institutions.

Non-bank financial institutions are a diverse and important faction of our financial sector. Many of these institutions provide short-term, small-dollar lending.

They enable families to purchase automobiles to take their kids to school. They provide the title insurance for those looking to purchase a home and move closer to the American dream. And they are often the lenders and service providers for basic consumer loans.

Yet, they are very different from community banks and credit unions: They don't use deposits to fund their operations.

As a result of this unique structure, they face operational challenges with which many on this committee may not be familiar. Today, I hope to explore a few of the more pressing regulatory issues facing these institutions.

First, the Consumer Financial Protection Bureau (CFPB) is in the process of integrating the Truth in Lending Act and the Real Estate Settlement Procedures Act into what will be known as TRID. This is a major endeavor that will significantly alter the mortgage closing processes for consumers, lenders, and title insurance companies. It is important for this committee to understand how the industry is working to comply with this August 1st effective date, and if there are issues the committee can help to address.

Second, the CFPB is in the process of promulgating rules addressing the short-term, small-dollar credit market. This market is widely used by the American consumer and is highly regulated and enforced at the State level. It is important for this committee to examine the regulatory structure of these products and to understand how the Federal regulators impact credit access and product choices for our consumers.

Third, the CFPB has taken significant regulatory action impacting the auto industry. While the Dodd-Frank Act exempted auto dealers from the CFPB's jurisdiction, the Bureau has tried to bypass that exemption by regulating the indirect auto lenders. The CFPB's actions have the ability to disrupt the automobile-buying

experience for consumers, and we have received bipartisan criticism that we will examine further.

Finally, it is important for this committee to better understand what the impact of Federal regulation and supervision means for industries historically regulated at the State level. While we often talk about regulatory burdens in compliance terms, burdensome, duplicative, and unnecessary supervision and examination can also be a burden to community-based lenders.

I am hopeful that the Members will leave this hearing with a better understanding of the current regulatory environment for non-depository institutions and areas of concern that the committee can address. We must push forward in our bipartisan efforts to provide regulatory relief for our Main Street financial institutions and protect the financial independence of the individuals and the families that they serve.

Now, I will recognize the ranking member of the subcommittee, Mr. Clay from Missouri, for 2 minutes.

Mr. CLAY. Thank you so much, Mr. Chairman.

And I also thank the ranking member of the full Financial Services Committee, Ranking Member Waters, for being here.

And to our witnesses, thank you for your participation today.

While the title of today's hearing sounds harmless enough, anyone who follows the work of our committee knows what this hearing is actually about: providing a venue to bolster the Majority's narrative that the Consumer Financial Protection Bureau is actually harming consumers by limiting their choices and freedom.

Prior to Dodd-Frank, consumers had ample freedom and choice. They had the freedom to choose risky mortgages with exotic products that eventually ravaged the economy.

For many of my constituents in St. Louis, they had the choice to support payday lenders that charge rates in the neighborhood of 455 percent. Or, as former Missouri Attorney General Nixon uncovered in Operation Taken for a Ride, thousands of Missourians were free to be misled into paying for extended service contracts on their vehicles that were deceptively marketed.

As so many of my constituents have come to learn, this kind of freedom is costly and serves as a constant reminder that the marketplace for consumer financial services can be treacherous for low- and moderate-income consumers.

This is particularly true in my home State of Missouri. With respect to payday lending, according to ProPublica, Missouri has about one payday or car title lender for every 4,100 residents, with short-term loans averaging 455 percent APR.

Statewide, a broad-based coalition of consumers' advocacy groups and community-based organizations tried to cap interest rates at 36 percent, but their efforts failed. And similar efforts around the country to regulate unaffordable short-term lending and abusive collection practices have fallen short until now.

I applaud the CFPB—is that 3 minutes or 5, Mr. Chairman?

I yield to the ranking member. I was just getting started.

Ms. WATERS. I will yield to the gentleman to complete his statement.

Mr. CLAY. Oh, thank you.

Only in Washington could a requirement that seeks to ensure that borrowers can actually pay back the money they borrow be considered a burden or controversial instead of sound underwriting. I find it odd that so often this committee only considers the cost of the CFPB's initiatives to industry without a fair and honest assessment of the benefits of the CFPB's work to consumers and to the economy.

Dollars not spent on unaffordable payday loans can often be spent on other goods and services that can spark economic activity, a consideration that rarely informs our discussion of the costs and benefits of Federal consumer protection laws.

Part of our job is to ensure that we strike the appropriate balance between the interests of industry and those of consumers. And the fact that this hearing is solely about the burdens on businesses, and only one witness is here to provide the perspective of consumers, speaks volumes on the Majority's imbalanced approach.

My concerns about the intentions notwithstanding, I remain committed to doing the difficult work of developing a regulatory approach that is properly calibrated to a firm's business model and risk profile. But this work of narrowly tailoring our regulatory approaches must be weighed against the very real risk that the business practices of non-banks pose to consumers.

I look forward to hearing from each of the witnesses.

Chairman NEUGEBAUER. And I thank the gentleman.

The distinguished ranking member of the full Financial Services Committee, the gentlewoman from California, Ms. Waters, is recognized for 1 minute.

Ms. WATERS. Thank you very much, Mr. Chairman.

And, Mr. Clay, I really appreciate the fact that we are having this hearing today.

While I have a prepared statement, I am going to deviate from that statement and simply say I am so pleased that we are going to talk about payday lending today. I am so pleased that we are going to talk about it because it is discussed everywhere throughout our communities, Members of Congress are talking about it, and we all talk about it in the way that Mr. Clay just described it.

We have constituents who, no fault of their own, don't earn very much money, don't have money for food or for their bills prior to their next payday, and they go to a payday lender and then they get hooked. They get hooked with 400-plus percent interest rates and, of course, they can't pay off the loan and so they resign them up, and it goes on and on and on. Once they get into debt with payday lenders, it is very hard to get out.

We have to change this. We have to do something about it. But I am very appreciative that the Consumer Financial Protection Bureau has finally announced its long-anticipated proposal to regulate the payday lending industry.

So I look forward to this hearing, and I thank you very much.

Chairman NEUGEBAUER. I thank the gentlewoman.

And I am now going to introduce our panel.

First, Ms. Paulina Sepulveda McGrath. Ms. McGrath is president and co-owner of Republic State Mortgage in Texas. She also serves

as the Chair of the Community Mortgage Lenders of America, which primarily advocates for non-bank mortgage lenders.

Ms. McGrath has led Republic since 1999, and during that time, Republic has grown from 2 to 22 locations in 7 States. Notably, Republic is the past recipient of the Inc 500 Award from Inc. Magazine. She also serves on the board of the Texas Mortgage Bankers Association and is vice president of the board of trustees of the Women's Fund, a nonprofit organization that provides Houston area women and girls with tools they need to—that can be advocates for their health.

I would like to now turn to the gentleman from California, Mr. Sherman, to introduce our second witness, Mr. Friedman.

Mr. SHERMAN. Yes. Justin Friedman is here from the American Financial Services Association. He served as my Legislative Advisor on the issues before this committee just a few years ago. When he left I told him, "You don't stop working for me; I just stop paying you."

But Justin's real genius was to give me advice on how to really make a witness squirm, how to make sure that their 5 minutes with me was one of the worst experiences of their life. And I hope that I have not lost those skills even though he has departed, and in a few minutes, we will find out.

I yield back.

Chairman NEUGEBAUER. I thank the gentleman.

Third, Ms. Diane Evans is vice president of Land Title Guarantee Company and serves as the president of the American Land Title Association, which advocates on behalf of the title insurance industry. Ms. Evans is active in the title industry both nationally as well as in her home State of Colorado. She has served on many State panels, including the State insurance title advisory panel; the State board of land commissioners, and in 2002 she was selected as Castle Rock, Colorado's Chamber of Commerce businessperson of the year.

Fourth, Mr. W. Dennis Shaul is CEO of the Community Financial Services Association, which is a national organization representing short-term, small-dollar lenders. Before joining CFSA, Mr. Shaul had a distinguished career on Capitol Hill as Senior Advisor to former Financial Services Committee Chairman Barney Frank.

Additionally, Mr. Shaul has served as the State of Ohio's chief financial regulator. Mr. Shaul earned his J.D. from Harvard Law School, and his Master's from Oxford University. He is a graduate of the University of Notre Dame, and he is also a Rhodes Scholar.

And fifth, Ms. Mitria Wilson is vice president of government affairs and senior counsel at the Center for Responsible Lending. Prior to joining the Center for Responsible Lending, she worked as the director of legislative and policy advocacy at the National Community Reinvestment Coalition.

Ms. Wilson specializes in the analysis of financial services issues, which focus on housing finance, student loans, consumer lending, and employment issues. In 2014 she was named as Woman of Influence by HousingWire Magazine.

Each of you will be recognized for 5 minutes to make your oral presentation. And without objection, your written testimony will be made a part of the record.

Ms. McGrath, you are recognized for 5 minutes.

**STATEMENT OF PAULINA SEPULVEDA MCGRATH, CHAIR, COMMUNITY MORTGAGE LENDERS OF AMERICA (CMLA)**

Ms. MCGRATH. Chairman Neugebauer and Ranking Member Clay, I am Paulina Sepulveda McGrath, president of Republic State Mortgage Company, based in Houston, Texas. I am here today as a chairperson of the Community Mortgage Lenders of America, a trade group representing both small mortgage bankers and community banks with mortgage lending experience.

CMLA supports the regulatory streamlining that Congress is moving ahead with for community banks. However, if the effort does not provide the same streamlining for all community-based mortgage lenders, including those that are not banks or bank affiliates, it will fail consumers and small businesses in every community in our country.

These unaffiliated lenders originated approximately 40 percent of all conventional loans and roughly 50 percent of all loans insured by the Federal Housing Administration and the Department of Veterans Affairs in 2014. We are a key piece of the mortgage market, especially for the first-time homebuyer and for those borrowers looking for or needing more personalized service.

Unfortunately, the current regulatory burden is driving consolidation among both community banks and small, unaffiliated mortgage lenders. If this consolidation continues, the resulting reduction in competition will lead to even higher costs and fewer choices for consumers.

As a Nation, we need to find a way to serve, with careful and safe underwriting, more families in their homeownership needs, particularly first-time homebuyers. If we cannot, these families will continue to pay ever-increasing rents that are outstripping income gains.

Remember, Dodd-Frank's goal was certainly to make lending safer for consumers. However, as we were told in 2009, the law was intended to regulate most closely the largest lenders and the bad actors.

Experience with this statute shows it lacks the flexibility to distinguish the level of regulation necessary for lenders of different sizes, business models, and performance records. Consequently, it levies the regulatory burden on everyone, including small lenders that operate in a prudent manner. Importantly, these small lenders simply cannot amortize large fixed costs onto a relatively modest volume of mortgage lending.

The CMLA would like to introduce a concept that will spur more community-based lending while not diminishing consumer protections. Why not provide some targeted relief for small lenders which have no recent enforcement actions and which originate primarily loans that meet the Qualified Mortgage standard contained in the truth-in-lending statute? Why not streamline certain regulations for these lenders, which recognizes their unique role in the lending

market and benefits the borrowers whose home financing needs they serve?

We propose that lenders receive specified regulatory relief so long as they remain: one, small; two, with most of their annual loan volume composed of QM loans; and three, only as long as they continue their excellent lending records.

If Congress adopted a framework like this, it would spur more community lending while maintaining the consumer focus intended by policymakers. This is most crucial for our country's underserved areas and communities, from the rural areas to the inner city.

CMLA recommends to Congress five steps to streamline current regulations. The first four steps are also supported by the Community Home Lenders Association (CHLA) a group of small lenders, all of which are unaffiliated with banks, that are working closely with us on these issues.

First: Eliminate the current 3-day waiting period between a revised disclosure and the closing of the loan if the revised disclosure has an APR for the consumer that is lower than the original disclosure.

Second: Exempt small lenders from the vendor oversight requirements.

Third: Direct the CFPB to concentrate their examinations on large lenders and those small lenders for which the CFPB has received a referral from another regulator, and exempt those small lenders that have no such referral.

Fourth: Refine the definition of "small servicer" to include those small lenders that subcontract part or all of the servicing function to a subservicer.

And fifth: Amend the SAFE Act to direct the issuance of a 180-day transitional license to registered bank-employed loan originators who were hired by an unaffiliated lender, which will permit these loan originators to continue to work while completing State licensing requirements.

The rationale for each of these proposals is set out in my written testimony. And of course, I will be happy to answer any questions you may have.

Thank you very much for this opportunity.

[The prepared statement of Ms. McGrath can be found on page 74 of the appendix.]

Chairman NEUGEBAUER. Thank you.

Mr. Friedman, you are recognized for 5 minutes.

**STATEMENT OF JUSTIN G. FRIEDMAN, DIRECTOR, GOVERNMENT AFFAIRS, AMERICAN FINANCIAL SERVICES ASSOCIATION (AFSA)**

Mr. FRIEDMAN. Mr. Chairman, Ranking Member Clay, and members of the subcommittee, good afternoon.

My name is Justin Friedman, and I am here on behalf of the American Financial Services Association. I am pleased to provide testimony as you examine regulatory relief for non-depository financial institutions and to discuss proposals to improve the structure of the Consumer Financial Protection Bureau.

I wish to thank the subcommittee for holding a hearing on this issue, which is of keen importance to the consumer credit industry and the households that we serve.

Founded in 1916, AFSA is the national trade association for consumer credit. Our 390 members include consumer finance companies, commercial banks, industrial banks, and other financial services companies that make credit available to consumers and small businesses.

AFSA members offer a broad array of financial products including personal installment loans, retail and commercial sales finance, credit and payment cards, residential mortgages, vehicle loans and leases, and floorplan finance for dealers. Our members provide approximately 80 percent of the Nation's vehicle financing. In general, finance companies are responsible for one of every five dollars of consumer credit in America.

While depository institutions play a vital role in the economy, Federal Reserve statistics show that a substantial share of consumer credit is provided by non-depository finance companies. In fact, for non-revolving lines of credit, finance companies and banks hold roughly equal shares of the pie—about one quarter each. Both are smaller than the share held by the Federal Government, which, of course, dominates the student loan market.

Finance companies have a long history of meeting the needs of consumers, such as buying or maintaining a car to get to work, or paying for higher education. Finance companies are licensed by each and every State where they do business. The CFPB has added a complex new layer of Federal oversight to the existing regime.

The principal types of credit offered by consumer finance companies are motor vehicle finance and traditional installment loans.

Lately, much has been said about the abuses found in certain forms of short-term, small-dollar lending. Policymakers should recognize that traditional installment loans are a time-tested and beneficial form of credit for working Americans, and they are based upon sound underwriting.

I am talking about fixed-rate, fully-amortizing personal loans, which are repaid in equal monthly installments of principal and interest. Traditional installment loans are the safest, most responsible form of small-dollar lending, and they have been for many decades.

AFSA members also offer motor vehicle financing: directly, through branch-based lending; and indirectly, through dealerships. Eight out of 10 consumers who finance their purchase of an automobile choose to do so at the dealer.

This financing is ultimately facilitated by the captive finance companies of the auto makers, independent finance companies, banks, and credit unions. Their provision of credit helps keep the auto market a strong, competitive, and integral part of the American economy.

While our industry is focused on providing a positive experience for the consumer, it also ensures a reliable source of liquidity for auto dealers. Specialized auto lenders do not withdraw from the market during economic downturns, unlike banks, that have safety and soundness concerns which may compel them to curb auto lending during times of turbulence.

The trope that non-depository lenders are unregulated is simply untrue. The creation of the CFPB imposes new, often duplicative Federal burdens on these State-regulated entities.

State regulators have a familiarity with local and regional circumstances. This knowledge, along with geographic proximity, means that a State regulator will often be the first to identify emerging issues, practices, or products that pose risks to consumers.

On behalf of AFSA's member companies, I wish to thank the committee for its help in enacting H.R. 5062, the Examination and Supervisory Privilege Parity Act last year. The Act clarified the law governing the sharing of information between Federal and State agencies that license, supervise, or examine non-banks offering consumer financial services.

This legislation resolved a regulatory disparity between depository and non-depository institutions, recognizing the unique situation of non-depositories and their relationships with State regulators. We are pleased that the legislation was passed in a bipartisan fashion, becoming the very first amendment to the CFPB statute that was enacted into law. AFSA hopes that this effort can serve as a model for future reforms to Dodd-Frank.

The CFPB's current governance structure is flawed, and it should be replaced by a bipartisan, multimember commission, as is the norm for virtually all independent regulatory agencies of the Federal Government. Unlike most of these agencies, the CFPB is headed by a single political appointee.

AFSA welcomes Chairman Neugebauer's introduction of H.R. 1266, the Financial Product Safety Commission Act, which alters the CFPB structure to be a five-member commission appointed by the President. While this is a step forward, the previous bills did not address State-licensed entities and the substantial portion of the consumer credit market that they serve.

As I noted previously, State regulators possess important insight into the practices and products of the lenders that they license. State regulators are best positioned to investigate issues that may pose risks to local consumers.

AFSA recommends that at least one member of the new board should have State bank or consumer credit supervisory experience. A similar approach has worked effectively at the FDIC, and it would be appropriate for the consumer regulator. Some fear that any structural reform would harm the mission of the CFPB, but AFSA believes an agency directed by a commission with staggered terms is better insulated from electoral politics and most likely to produce sustainable policy that will protect consumers while promoting access to credit.

Thank you.

[The prepared statement of Mr. Friedman can be found on page 66 of the appendix.]

Chairman NEUGEBAUER. Ms. Evans, you are recognized for 5 minutes.

**STATEMENT OF DIANE EVANS, PRESIDENT, AMERICAN LAND TITLE ASSOCIATION (ALTA)**

Ms. EVANS. Thank you, sir.

Chairman Neugebauer, Ranking Member Clay, and members of the subcommittee, thank you for inviting me here today. My name is Diane Evans and I am vice president of Land Title Guarantee Company in Denver, Colorado. Along with my day job, I serve as the president of the American Land Title Association.

ALTA is a national trade association that represents the abstractors, settlement service providers, and title industry across this United States. ALTA has more than 5,500 member companies ranging from small, one-person operations to large, publicly traded companies. Our industry employs more than 108,000 professionals, and we have offices in every county in this United States.

I am happy to be here today to discuss how overregulation is affecting our industry, our members, and our consumers. As you know, the Dodd-Frank Act required the CFPB to combine the disclosures required under the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA) into a single TILA–RESPA form, which we commonly call TRID.

The Bureau started this process back in 2011, and we implement these new disclosures on August 1st, 107 days from today. We know that the ultimate purpose of TRID is to help consumers better understand their real estate transaction, and that is extremely important to our members, who are sitting across from homebuyers while we are sitting here today.

We have three primary concerns. First, our experience in implementing regulation tells us that there will be unforeseen issues once we start using these forms in actual, real transactions. To assist with this process, ALTA requests that the CFPB publicly commit to a hold-harmless period of enforcement from August 1st through the end of the year.

I thank Chairman Neugebauer and Congressman Luetkemeyer for their leadership in asking CFPB Director Cordray for that hold-harmless period, and I request that the rest of the subcommittee follow that lead. A hold-harmless period in the first few months allows industry to adapt their business processes to comply with the regulation without fear of enforcement action or potential class action lawsuits. It allows us to focus on our business, our customer, and the consumer.

Second, this new regulation prohibits the industry from disclosing the actual cost of a title insurance policy purchased by the consumer at the closing. Consumers will be confused because the government-mandated form will disclose different prices than the actual cost that consumer will pay at the closing table. They will be unable to shop using accurate cost analysis.

The Bureau should resolve this issue by requiring us to disclose what the actual title insurance premium is on each transaction as required in each individual State.

Finally, a 2012 service provider bulletin, which was issued by the CFPB, continues to cause uncertainty in the marketplace for our members. Unlike the CFPB, other Federal regulators have provided helpful guidance so that businesses understand how to manage the risks associated with third-party service providers. Lenders are left without this clear guidance on the appropriate risk management procedures that they need for their title and settlement service providers in this industry.

In 2012, due to the lack of that additional guidance, ALTA developed the title insurance and settlement company best practices. These were created to help our members highlight policies and procedures that our industry exercises to protect lenders and consumers while ensuring a positive and compliant real estate transaction.

To improve the way the CFPB works with and provides information to businesses, I urge Congress to pass H.R. 1195, the Bureau of Consumer Financial Protection Advisory Boards Act, as soon as possible. Thank you to Congressmen Pittenger and Heck for their leadership in sponsoring this bipartisan legislation that establishes a small business advisory board at the CFPB. It provides those open and formal channels of communication from CFPB staff in this industry.

I appreciate the opportunity to be here and I look forward to serving as a resource and answering questions for you all. Thank you.

[The prepared statement of Ms. Evans can be found on page 55 of the appendix.]

Chairman NEUGEBAUER. Thank you.

Mr. Shaul, you are recognized for 5 minutes.

**STATEMENT OF W. DENNIS SHAUL, CHIEF EXECUTIVE OFFICER, COMMUNITY FINANCIAL SERVICES ASSOCIATION OF AMERICA (CFSA)**

Mr. SHAUL. Chairman Neugebauer, Ranking Member Clay, thank you for inviting me to testify, and I look forward to questions that you may have.

I am the chief executive officer of the Community Financial Services Association of America, an entity which represents non-depository financial institutions and includes more than half of the storefront payday loan entities across the country.

We are particularly interested in CFPB's recent proposals with regard to our industry and companion industries that are in the short-term, small-dollar market. I look forward to these with particular interest because, as was mentioned a while ago, I was here as a staff member during the drafting of Dodd-Frank and participated in that capacity and I have looked forward to working with the CFPB.

That has not always been easy, and it is in part what draws me here today.

It is important, I think, to note at the outset that the concept was, for me, one that was laudatory. The practices may not meet the measure that I had hoped, and I think others had hoped, they would meet.

So it was with some real anxiety that we began to look at the paper that was propounded approximately 2 weeks ago by CFPB relative to our industry and companion industries. That raised several questions for us.

In terms of the immediate future, that document goes to the Small Business Regulatory Enforcement Fairness Act (SBREFA). And it is important because the Bureau describes it as the entry point for regulation of large and small entities.

The reason I am discouraged is that as I read that paper, and by the admission of CFPB, it would put out of business approximately 60 percent of those in the small business area. Now, CFPB uses the language that so often accompanies the closing of plants and the displacement of jobs. They speak about it as—in the bloodless way of saying that there is going to be consolidation within the industry.

Make no mistake. It isn't consolidation we are talking about; it is job loss, and 50 percent of those jobs have medical benefits, et cetera.

So we are concerned about that. And we are concerned whether this isn't an entree to throw the baby out with the bath water.

As we look at the statistics propounded by CFPB, we understand that they have a particular concern for people who are in the product payday too long, but it is not necessary to throw out the product itself to get at those who need consumer protection. And I think it is instructive to remember that two Federal banks—the New York Reserve and the Kansas City Reserve—have spoken about the indirect and unintended consequences of restricting payday lending.

I am not at all sure that the research that the CFPB has done on this topic is meritorious in two senses. First, it may not have begun with the proper question, which I believe was, given a sample of people who use payday loans, how many of them benefit from them? How many are neutrally affected? And how many are worse off?

And clearly, the task is to work with those who are worse off and make certain that they either do not acquire payday loans, or make certain that they are given ample consumer protection if they do.

This is a complicated area, and you must recognize that every entity that we represent is State-licensed and must also undergo the test of our own better business—better practices. That means, in effect, something that was not taken into account by CFPB: There are distinguishing characteristics in this area between those online, between those in storefront, between those in title lending, between those who are large and those who are small, between what applies in Florida and what applies in California.

The Federal system was once described by Justice Brandeis as providing a laboratory for experimentation. What the CFPB is about to do is close the laboratory and make a one-size-fits-all set of demands on all those who are participating as operators for this product and for the customers.

I speak today as much for the customers as I do for our operators, and I would encourage any of you who have doubts about the efficacy of what we do to visit our stores and see how the customer comes out of our place.

It seems to me that it is important to provide consumer protections. It seems to me also that regulating payday is not a path to annihilation, as it apparently is to the Bureau at this point.

[The prepared statement of Mr. Shaul can be found on page 81 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman.

And now, Ms. Wilson, you are recognized for 5 minutes.

**STATEMENT OF MITRIA WILSON, VICE PRESIDENT, GOVERNMENT AFFAIRS, AND SENIOR COUNSEL, CENTER FOR RESPONSIBLE LENDING (CRL)**

Ms. WILSON. Good afternoon, and thank you, Chairman Neugebauer and Ranking Member Clay, for this opportunity to testify today.

I have had the opportunity to benefit from hearing all of the other panelists who went before me, and one of the things that I thought was really striking about the invitation to testify today was that the request itself asked us to focus on community financial institutions. And there is something special about community financial institutions, and that is a fact that the Center for Responsible Lending patently recognizes.

Community financial institutions are actually based on a business model that recognizes relationships and the importance of relationships with consumers. So it is with that being understood that I have to tell you that today I actually came to be a counterpoint to most of the assertions that are being made by the prior panelists.

We value community financial institutions because we believe that they create choice, opportunity, and access, and they proliferate the ability to generate competition that drives down prices for consumers.

I have to tell you that most of the proposals that are being advanced today have little to do with either of these objectives and principles, and for that reason they should be opposed.

For example, one of the points that we have talked about today was the importance of auto lenders and indirect auto financing. And people suggest that this is a question of opportunity, that financiers should be able to actually charge an increased commission based on the interest rate without any consideration and that should be okay.

But the reality is that evidence shows that the way in which auto financiers do that, dealers, lends itself to a result that actually shows discriminatory practices—that is that people of color, people of low- and moderate-income backgrounds, are those who are most likely to actually receive an interest rate markup.

That kind of opportunity is not an opportunity at all. It is discrimination and it is illegal under the Equal Credit Opportunity Act.

So to the extent that the Consumer Financial Protection Bureau's bulletin actually recommended that auto financers and lenders who had an indirect relationship stray away from that kind of practice and policy, we believe that was actually a responsible recommendation by a Bureau that has been charged with enforcing the Equal Credit Opportunity Act.

And now to choice. One of the most fascinating things about our conversation around expanding access to credit has been an argument that non-depository mortgage lenders are somehow in a position of being disadvantaged by the regulations that—created by the ability to repay rule.

We think it is a simple concept that is basic to business that, in fact, if you are going to underwrite a loan you should make sure that the individual to whom you give that loan has the ability to

repay it. There is nothing novel about that; it is a common-sense approach.

So then the question becomes, are there other ways that non-depositories or smaller financial institutions can satisfy that burden without having the same in costs? The reality is for non-depository financial institutions, they have adapted and accepted a business model that far more parallels larger financial institutions than what we think of as traditional community banks.

I would suggest to you that a non-depository institution does not, in fact, have a long-term relationship with the consumer. Why? Because a mortgage lender who is a non-depository doesn't have interactions with the consumer on multiple bases. They are making a one-time loan to that consumer.

And interestingly enough, unlike what we think of as traditional community banks, non-depository mortgage lenders are not located in communities, by and large. A great example of that is Freedom Mortgage, which, although being located in 8 different States, actually offers mortgages in 50 States across the country.

I think that most Americans listening to this conversation today would be hard-pressed to agree that an institution making a loan in the State of Texas that is based in New Jersey somehow understands community banking and relationship lending.

Thank you for the opportunity to testify, and I am happy to answer any questions that you may have.

[The prepared statement of Ms. Wilson can be found on page 94 of the appendix.]

Chairman NEUGEBAUER. I thank the gentlelady.

And now, each Member will be recognized for 5 minutes for a question-and-answer period.

I will begin by recognizing myself for 5 minutes.

As has been mentioned, the CFPB finalized rules that combined the disclosures that consumers receive both at applying for and closing their residential loans, the Truth in Lending Act and the Real Estate Settlement Procedures Act. Now, I am quite honestly supportive of simplifying the forms. As a former—I have been in the real estate business for a long time and the forms have increased dramatically, and so somehow harmonizing that I think is a good process.

But I have heard from the industry representatives that with the rules that came along with this new form—I think it was over 1,000 pages, if I am not mistaken—there are a lot of other details that go with using that form together.

Ms. Evans, can you kind of describe some of the challenges that you are facing as you approach this August 1st deadline for complying with the new rules, at the same time implementing the new form?

Ms. EVANS. Thank you, Chairman Neugebauer.

Yes. There is much more to this process than just forms; it is about a whole paradigm shift on how transactions are going to be closed. And we absolutely agree that a better-informed consumer is far more educated to make good, solid decisions about their financial obligations.

The new forms are very costly to title insurance companies large and small. It requires a total new process. In fact, many of our

companies are having to upgrade and redesign their entire systems to accommodate the rule that was put forward, and to a very small operation across the Nation that we have, it could be a matter of whether they are going to make money or lose money this year.

We are committed to making sure that consumers are able to close their loans, that real estate transactions go forward. But the one big issue still looming is the calculation or the miscalculation, as the rule requires, of the title insurance costs for consumers.

Chairman NEUGEBAUER. Ms. McGrath, on your side of the process, how is this impacting you?

Ms. MCGRATH. We completely agree that it has been a very confusing and challenging process for companies of all sizes, but in particular for smaller lenders. We are absolutely having to change all of our systems, and in many instances we are at the mercy of our loan origination system providers, who are having to put together this information and haven't yet completed the process.

So we absolutely agree that a non-enforcement period through the end of the year would be incredibly beneficial. We are doing everything we can to educate our employees and work together with our partners at the title companies and our REALTOR® partners to help to educate the consumer and prepare for what is coming, but at the end of the day, this is going to be a very challenging process and it is just going to hurt consumers who are trying to buy their homes.

Chairman NEUGEBAUER. Yes, as I think was mentioned, Mr. Luetkemeyer and I sent a letter requesting that kind of a hold-harmless period here beginning August 1st, and one of the reasons I agreed to do that was that from my days in the homebuilding business and the real estate business, August was a big month. In other words, families were trying to close their new home purchase so that they were changing school districts and so it was important to do that.

What I began to worry about when we—because really the purpose of this hearing is to talk about how this is impacting the American families and consumers, and what I am worried about is that we come up to that August period of time and people are trying to work out the glitches in their system, and then a last-minute charge comes in and that closing may have to be delayed because now the title company, for example, or the lender is afraid to give authorization to close that loan until they have gone back and double checked.

Is that a reality?

Ms. WILSON. Chairman Neugebauer?

Chairman NEUGEBAUER. Just a second. I was—Ms. Evans?

Ms. EVANS. Thank you, sir. Yes.

And one of the most challenging aspects with a hard start period or a hard stop, however you would like to couch it, is the fact that we are going to be faced with closing loans under the current process as well as those loans that will close under the new process, because the rule very specifically defines applications made on or before August 1st will close under the current process; applications made or closed after August 1st and thereafter will close under the other process.

And so both title entities and lenders are forced to maintain dual operating systems for who knows how long in order to make sure that consumer is well-served and those transactions can close during a most busy time of the year.

Chairman NEUGEBAUER. My time has expired.

The gentleman from Missouri, Mr. Clay, is recognized for 5 minutes.

Mr. CLAY. Thank you, Mr. Chairman.

Let me start with Ms. Wilson. In addition to serving as a consumer advocacy organization, the Center for Responsible Lending also provides alternatives to payday lending.

In CRL's experience, have your alternative products been profitable?

Ms. WILSON. They have. One of the benefits of being an employee of the Center for Responsible Lending is that not only do we advocate or do research on financial services, but we are an affiliate of Self-Help, a credit union based in North Carolina, Illinois, and California. We actually provide products and services to consumers across the country, and so we understand the business model of community bank lending.

The Center for Responsible Lending, through our relationship with Self-Help, has been able to determine that you don't have to charge 300 percent or 400 percent interest rates to do business with working-class individuals across the country in order to do short-term loans. In reality—

Mr. CLAY. And you can still be profitable.

Ms. WILSON. Right, and be profitable. In reality, you can charge interest rates that are well below proposals like those existing in the Senate that suggest a 36 percent rate cap. In fact, for the Center for Responsible Lender's affiliate, Self-Help, our interest rate on short-term loans is approximately 25 percent.

Mr. CLAY. Thank you for that response.

Mr. Shaul, Federal law establishes an ability-to-repay standard for credit cards and mortgages. Should payday lenders have to abide by a similar standard?

Mr. SHAUL. They certainly should have to abide by an ability-to-repay standard, no question. When we were present at the CFPB for interviews and discussions, I think the staff was generally amazed that there was in place already a lot of the standards necessary for ability to repay.

This is an ongoing discussion of what would constitute exactly the criteria for ability to repay, but I think it is an unassailable proposition that everyone should be given criteria by which we would assess whether or not they can repay a loan.

Mr. CLAY. So you think your industry will come up with a bright line that says, "Okay, these are the standards, this is what a person has the ability to repay us on a monthly or weekly basis," and then it will be accepted universally by the industry?

Mr. SHAUL. Congressman Clay, I have learned the hard way that this is a very diverse industry, and I would never attempt to speak for everyone within it. I would say that our members, who are, I think, committed to a higher standard and to reform, are completely willing to take up the issue of ability to repay, work with

the Bureau on it, and come to a conclusion that I think could be accepted by everyone within our membership.

Mr. CLAY. Okay. That is a fair response.

Let me ask you about—in light of CFPB's enforcement actions and supervisory highlights of the payday lending industry, why do you still believe that State regulation provides adequate protection for consumers nationally?

Mr. SHAUL. In part because when Director Cordray appeared before the Financial Services Committee and gave testimony, he was pressed on the question of which States had fallen down in providing adequate safeguards for consumers, and he did not really reply to that. It is hard to convey exactly all of the differences that exist State by State within the payday empire.

There are some 15 States that do not have payday at all. There are States that have what they denominate as strict regulation. California really has a payday loan that amounts to $270, $273. Florida has a very different situation from that.

The analysis that should be done and that we recommend to the Bureau is to take each of the States that have a payday component and determine what needs to be preempted by the Bureau because there is a specific weakness or specific problem within it.

I am concerned about preemption because one of the models that is being put forward as an exhibit—a good exhibit—is Colorado, but there doesn't seem to be an appreciation that you don't get to the Colorado model unless you have the ability within the States to experiment, make determinations on their own, and out of the best of that we can come up with a comprehensive set of norms that I think would serve the industry well.

Mr. CLAY. Thank you for that response.

Okay, my time—

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from New Mexico, the co-chairman of the subcmmittee, Mr. Pearce, is recognized for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

And thanks to each one of you for your presentations.

Ms. McGrath, you may have heard Ms. Wilson. She said that the mortgage lenders basically don't have relationships or, she leaned that way—she may not have said that exactly. Is that true? Mortgage lenders don't have relationships with their customers?

Ms. MCGRATH. I don't believe that is true at all. As a matter of fact, our company is built on the relationships that we have built with REALTORS® and our customers. That is how we receive our loans.

Mr. PEARCE. Your customers come back and finance—

Ms. MCGRATH. Absolutely. We—

Mr. PEARCE. —a different house—this is not one time out?

Ms. MCGRATH. Yes, sir. We regularly see customers come back and then refer their friends to us. We actually spend very little relative to our overall expenses on advertising because we get referrals from our existing customers time and time again.

Mr. PEARCE. Okay. If the coming regulations are going to put pressure on the industry, will that pressure be greater on the smaller, local institutions or greater on the large, international, national mortgage banks?

Ms. MCGRATH. Sir, at the end of the day, the regulations that are in place right now have had a tremendous impact in terms of fixed costs and per-loan costs. The larger banks—

Mr. PEARCE. So it would be tougher on the smaller—

Ms. MCGRATH. It is much tougher on the smaller—

Mr. PEARCE. So what Ms. Wilson is recommending, that we go along with CFPB and just act like it is all good, actually will ensure that what she says is already happening would actually happen. It will force the small people out of the market and you will just be left with the big guys that can afford to come in with the cost.

Ms. Wilson, have you all studied the payday lending—your center?

Ms. WILSON. Definitely. The Center for Responsible Lending has—

Mr. PEARCE. What would be a fair percentage rate—you said we don't have to charge the high rates, and I understand the ranking member and Mr. Clay both have pointed out shortcomings of the system, and we would acknowledge that those shouldn't exist, but what would be a fair percentage to charge? You said you studied it and you said you researched it, so—

Ms. WILSON. Right. One of the things that I would point you to is actually—

Mr. PEARCE. Ten percent? Twenty percent?

Ms. WILSON. There is legislation, actually, in the Senate, introduced by Senators Durbin and Merkley that set the rate cap of 36 percent.

Mr. PEARCE. No, I mean, what is your opinion? What is your group's opinion that a fair rate is? Ten percent?

Ms. WILSON. I think we support the 36 percent rate cap that Senators Durbin and Merkley—

Mr. PEARCE. So, 36 percent. We will just call it 40 percent. Fair enough?

Ms. WILSON. I think a 36 percent rate cap is—

Mr. PEARCE. Okay. Call it 30 percent. We will go low then—30 percent.

So the average guy in the oil field whom I represent comes to me and asks me, "What business is it of yours, the government, if I want to borrow $100 today and pay back $120 at the end of the week? What business is it of yours?"

But if we apply your standard of 30 percent, basically for that $100 the lender is going to get 36—yes, basically 30 cents. So you loan $100 for a week, you get 30 cents back. That is 10 percent is $10 over a year and then just divide by 52. That is not exactly scientific, it is not exactly perfect, but it is close enough for the discussion.

So would you loan $100 for a week for 30 cents?

Ms. WILSON. Well, Congressman—

Mr. PEARCE. No, I am just asking a straight question. It is easy. It is either yes or no, and I don't think you would. And I don't think you could make any money at it.

And so what you are going to do is you are going to force these people out of business by putting these caps on here, and at the end of the day the guy borrowing the money asks, "What business

is it of the government if I want to borrow $100 to get me through to the next payday?" But you would choke that opportunity off.

And I am not trying to attack you, because it is not you. But it is people who declare what is and what isn't and the whole circumstance of loaning money.

So, Ms. Evans, I get complaints from the community banks a lot that this has made life very difficult for them—the CFPB, the QM rule, all that. Have you noticed any change in the offerings from community banks as far as the lending to real estate purchases?

Ms. EVANS. What we have noticed is conversations about, I don't know whether I am going to be able to offer mortgages in my small markets. What is the consequence going to be, and can I afford either the implementation or the risk of—

Mr. PEARCE. And so if that is the case, if people choke that off, who are going to be the losers? Who cannot go find a different market?

Ms. EVANS. The small community—

Mr. PEARCE. The small communities, the poor people, the people who are at the bottom end of the economic spectrum will have no other choices. And so we are—we have people of good will—Ms. Wilson I consider to be of tremendously good will—but they are suggesting things which are going to choke off access to the poor, to the people who are not in large markets because no bank in New York is ever going to come into the 2nd District of New Mexico and loan for a $30,000 house. I will guarantee it. And so, you will choke off those people.

So I appreciate your good heart in the deal, Ms. Wilson, but I really see a different side of the argument.

Thank you very much. I yield back.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from Georgia, Mr. Scott, is recognized for 5 minutes.

Mr. SCOTT. Yes. I would like to direct my question to Mr. Friedman.

There has been much discussion about the CFPB's governance model, whether we should have a single director or a multi-commission for its governance. Can you explain to the committee what would be the shortcomings of the CFPB's current governance that could be cured by replacing a single director with a multimember commission?

Mr. FRIEDMAN. Thanks for that question, Congressman.

Most Federal regulators, independent regulators, are headed by a bipartisan, multimember commission, and what we find is in those cases they are more deliberative about the policy they put forward. It is not just about approving rulemaking, but also which enforcement actions they take up.

By having a multimember commission you set up a process by which staff at the agency has to put forward a proposal and the members consider it and often take a vote on whether to proceed. In the case of a single political appointee, it is really just a matter of a memo to the boss and he will sign off on whether to move forward or not, and there is no public record or transparency in how that decision is made.

Mr. SCOTT. So in your opinion, what would be the best method? Which way should we go—single director or multimember commission?

Mr. FRIEDMAN. AFSA would recommend a multi-member, bipartisan commission with staggered terms, allowing a new President, as he came in, to appoint the chairman, and having that institutional memory holdover. It also provides an avenue for stakeholders like our industry and like consumer advocates and like Congress, to approach the various commissioners and bring their issues to the fore.

Mr. SCOTT. And what benefits would this bring to our financial services industry?

Mr. FRIEDMAN. Ultimately, I think that it would promote better policymaking that carefully weighs consumer protections against the need to ensure access to credit, particularly for financially underserved Americans, who are the ones who are more commonly served by non-banks.

Mr. SCOTT. Let me ask you another question, if I may. Consumer finance companies differ from banks and from credit unions, which is why they have been regulated differently. Finance companies, for example, do not accept deposits, so they are not supervised for safety and soundness.

So why is it important for a consumer regulator to concern himself or herself with this distinction?

Mr. FRIEDMAN. Sir, safety and soundness concerns for banks and credit unions are very real. Consumers put deposits at those institutions and the government has a stake in ensuring that they are not lost if the institution fails.

In the case of a consumer finance company, they are lending out of their own capital, and if the institution were to fail then the portfolio of loans would be bought up by some other institution which would continue to collect the payments. But no consumers would lose their nest egg.

As a result, consumer finance companies are able to take risks that depository institutions are not, and that means that consumers who are lower down on the credit spectrum, perhaps have dings on their credit histories, are able to find loans from consumer finance companies that they might not get from a depository institution.

Mr. SCOTT. Thank you.

Ms. Wilson, you are with the neighborhood lending group, is that correct? Is that the group out of North Carolina? I'm sorry.

Ms. WILSON. The Center for Responsible Lending?

Mr. SCOTT. The Center for Responsible Lending. Is that the one out of North Carolina? Are you based out of North Carolina, or—

Ms. WILSON. CRL is actually the national headquarters in Washington, D.C., but we are affiliated with Self-Help, which is, in fact, based in North Carolina.

Mr. SCOTT. Okay. Tell me what your assessment is. You have followed our work here. We had a program on mortgage lending. It was called the Hardest Hit program.

Are you familiar with that, where we put that into the Wall Street bailout—and I hate to use the word "bailout"—program? But

it was able to go down and help struggling homeowners in the hardest-hit States with unemployment and mortgage foreclosures.

And I wanted to just get your assessment on how you feel that program has helped in the lending area, particularly for those behind on their mortgages.

Ms. WILSON. Certainly. The Hardest Hit Fund was actually intended for very good reasons, to direct capital to stem the challenges that were facing communities that were really burdened by the impact of the housing crisis and the market's implosion.

There have been challenges with the program, and there is no denying that. Mostly those challenges have actually related to the restrictions that exist on the ability to release those funds. So there are remaining funds that we hope that we can actually get released.

Chairman NEUGEBAUER. The time of the gentleman has expired.

The gentleman from North Carolina, Mr. Pittenger, is recognized for 5 minutes.

Mr. PITTENGER. Thank you, Mr. Chairman.

Ms. Wilson, I think it is fair to say that you have a strong aversion against payday lending. You don't like payday lending. You think it harms people. Is that right?

Ms. WILSON. Let me say this: I think short-term lending can be a very beneficial product and a necessary product, but I do take exception to payday lending to the extent—

Mr. PITTENGER. Payday lending, as it is today, harms people.

Ms. WILSON. —that it has a 400 percent or 300 percent interest rate.

Mr. PITTENGER. Reclaiming my time, yes or no: Payday lending, as you see it today, harms people, is that right?

Ms. WILSON. Short-term lending can be very beneficial.

Mr. PITTENGER. Payday lending harms people. Okay. I understand.

Ms. WILSON. 400 percent interest rates harm people. I would agree with that.

Mr. PITTENGER. I appreciate that. Now, you are moved by a personal concern, is that right? You care about people. And I value that. I respect that.

Ms. Wilson, I would ask you, do you smoke?

Ms. WILSON. I don't.

Mr. PITTENGER. There are people who smoke.

Ms. WILSON. I know.

Mr. PITTENGER. There are warning labels on smoking cigarettes that warn people they could die. Isn't that right? We allow people freedom to make a choice. Is that correct?

Ms. WILSON. That is correct.

Mr. PITTENGER. Ms. Wilson, do you drink alcohol?

Ms. WILSON. I do occasionally.

Mr. PITTENGER. Okay. The ranking member mentioned that people get hooked on payday lending. Some people get hooked on alcohol, don't they? Do we allow alcohol?

Ms. WILSON. We do.

Mr. PITTENGER. We do.

Ms. Wilson, do you eat products with sugar?

Ms. WILSON. That is a really personal question.

Mr. PITTENGER. I know.

Ms. WILSON. I am going to tell you right now—

Mr. PITTENGER. I know, and if a—

Ms. WILSON. —that I do.

Mr. PITTENGER. My doctor—

Ms. WILSON. I will admit it today before you.

Mr. PITTENGER. And we are hearing the stats all the time that diabetes is the number one health problem we have right behind heart problems. A lot of people get hooked on sugar.

You know, Ms. Wilson, people marry who they want to marry. And sometimes, they marry bad people. I have met some of those, maybe you have, but they made that choice. People make choices.

Do you believe in Big Brother?

Ms. WILSON. Do I believe in—

Mr. PITTENGER. Do you believe in Big Brother—should Big Brother determine what choices people can make?

Ms. WILSON. Representative, what I would say to you is that when it comes to financial services, the Federal Government and State governments have recognized that usury is a problem—

Mr. PITTENGER. And we recognize—

Ms. WILSON. —and the question that we are asking about—

Mr. PITTENGER. Reclaiming my time—

Ms. WILSON. —payday lending is whether or not usurious rates should be something that is acceptable. And the law has a long-standing—

Mr. PITTENGER. Ms. Wilson, with all due respect—

Ms. WILSON. —of rejecting that.

Mr. PITTENGER. —is smoking not a problem? Is alcohol not a problem? And for many people, sugar? Do people get hooked on these?

Ms. WILSON. They do, but it is regulated by the Federal Government—

Mr. PITTENGER. And they make choices. And we have given warnings. There are disclaimers.

I think we have made our point, haven't we?

Ms. Evans, you made a wonderful statement about the legislation that my colleague, Mr. Heck, and I have introduced on a small business advisory board for CFPB, to ensure that small businesses who work with financial services products have a voice at the table. What would you say to your critics—maybe those with the Center for Responsible Lending here today—who claim H.R. 1195 is redundant and not needed?

Do you feel like we need to have that voice? Is there pressure on small businesses that they need to be able to have that forum?

Are there compliance problems that maybe the CFPB needs to know about? Give me some of your responses to that.

Ms. EVANS. Sir, thank you for asking. Yes, absolutely.

Small businesses, medium-sized businesses all need a voice with the CFPB and a way to communicate about the consequence of overregulation to the cost of business and their ability to engage with consumers in their local market. And H.R. 1195 gives that voice to small business.

Mr. PITTENGER. Thank you.

I reserve the balance of my time.

Chairman NEUGEBAUER. I thank the gentleman.

The gentleman from Washington, Mr. Heck, is recognized for 5 minutes.

Mr. HECK. Thank you, Mr. Chairman.

I worked long and hard with Mr. Pittenger on the non-bank advisory board. I had hoped it would pass. I worked long and hard with Mr. Posey on the advisory opinion board.

But, as Mr. Pittenger knows full well—and I compliment him again for introducing the bill—an amendment was added yesterday that kills the bill. It is dead.

It may pass the House, I don't know, but it is dead. It is dead, of course, because the bill was used as a vehicle after it got out of committee for another purpose, and that is to harm the CFPB.

I suppose my question for those of you who want to and seek increased collaboration between the regulated parties and the regulator would be, how can those of us who think that is appropriate work and proceed in order to have the same outcome?

Because let me repeat—Ms. Evans, I think I would like to start with you—that bill is dead. And it is my bill, so please understand—along with Mr. Pittenger, the lead—I take absolutely no pleasure. In fact, it grieves me deeply that this has occurred.

What do you want us to do when we are confronted with this? We are trying to be helpful and constructive. How can we do that?

Ms. EVANS. My response would be that we all, as businesses, work together in order to make sure that consumers are able to obtain mortgage loans, they are able to buy homes for their families. And I would urge each and every one of you, irregardless of the side of the aisle that you are on, to work together to make sure that we as small businesses—my members, my company in Colorado, and each of us that employ citizens in our communities and help drive healthy and successful communities, you need to come together and find a solution.

You need to help us out. We are the bedrock of this United States and we are depending on you to come up with a solution to keep us in business.

Mr. HECK. Hear, hear, Ms. Evans.

Please note the bill came out of committee 53 to 5, and after it got out of committee, without consultation across the aisle, the amendment was proposed. So we collaborated—for months we collaborated. And we are deeply frustrated.

And if I am conveying the depth of my frustration to you—and all of you who wanted this bill to pass, including myself—please understand how deep my frustration is that after months of working on this, we were bushwhacked.

Ms. Wilson, I have, admittedly, a lot of sympathy for the concerns that have been expressed about the difficulties in implementing the August 1st deadline and the integration of TILA and RESPA. I frankly think they are right, that it is a deadline that may be problematic.

But I am interested in your response. Please know that we may have a little bit of a disagreement if you are going to come from where I think you are, but I do want to know what your point of view is.

Ms. WILSON. I am so glad that you asked me that question. I wanted to have the opportunity to speak to that, because I think this is actually a really fascinating issue for one particular reason.

The integrated disclosure requirements were actually implemented by a final rulemaking by the CFPB in 2013. So the rules that were actually supposed to guide this process the industry has had notice of for almost 2 years.

In the timeframe between that, the Consumer Financial Protection Bureau has done four webinars, has released seven different consumer guides, business guides, small business compliance guides. They have actually done eight forms specific to the different types of mortgage loans that could take place to show the disclosures.

And at the end of the day, the rule itself is not a rule that actually assesses a different burden, but is intended to actually decrease the number of forms that the industry has to provide.

Why am I saying this? I am saying this because just less than a year ago the very same industry associations that are coming to you today and asking you for an extension testified before this very same subcommittee that the very rulemaking that the CFPB engaged in with respect to the integrated disclosure should be hailed as a classic example of how the industry can work with the CFPB to get the rule and the process right.

Mr. HECK. Okay. I see the yellow light is on so I don't mean to rudely interrupt, but—

Ms. WILSON. Yes.

Mr. HECK. —frankly, you haven't swayed me. But in my limited time left I would be interested in hearing a rebuttal from industry as to why, given that context, you think we just all didn't—Mr. Chairman, I want to register my objection to the absence of clocks in our temporary hearing room, which did not enable me to calibrate my question. Thank you.

Chairman NEUGEBAUER. The gentleman's comment is noted. I can't do anything about it, but it is noted.

The Chair now recognizes the gentleman from Texas, Mr. Williams, for 5 minutes.

Mr. WILLIAMS. Thank you, Mr. Chairman.

And I thank the witnesses for being here today.

In full disclosure, I must say the following: I am from Texas. I am a small business owner, 45 years—family 76 years. I have enjoyed this testimony.

And I am a car dealer, new and used. And I think Dodd-Frank is just about the worst legislation we could ever have.

Now, with that being said, I want to direct my first set of questions to Mr. Friedman.

The first is almost the same question I asked Dr. Cordray a few weeks back when he testified before our committee, but hopefully—and I feel like I will—I will get a more detailed answer from you. Under the Dodd-Frank Act, does the CFPB have statutory authority to regulate auto dealers?

Mr. FRIEDMAN. No, sir.

Mr. WILLIAMS. Elizabeth Warren is out there today saying they do, so we will have some interesting debate.

Second, is it your opinion that CFPB is indirectly regulating auto dealers' behavior by holding lenders accountable for dealers' actions, something they cannot control?

Mr. FRIEDMAN. Yes, sir.

Mr. WILLIAMS. Okay. Now, Director Cordray has insinuated that auto dealers base financing rates on eyeballing a customer and that this practice was regrettable. Basically, he is saying that in my industry and in my business we charge different rates based on someone's ethnicity, skin color, gender, and so forth.

I know that AFSA commissioned a study that studied the methodology used by CFPB to determine disparate impact and it has significant error rates. So the question is, is the CFPB putting dealers in an impossible position here by saying that their lending policies may be discriminatory, yet not giving them any guidance on how to avoid potential liability?

Mr. FRIEDMAN. Yes, I would agree with that, sir. And I would add that our industry has zero tolerance for discrimination, and we are eager to work with the CFPB and the Department of Justice and any other stakeholder who cares about fair lending.

We simply disagree with their methodology and the approach they have taken, and we also disagree with the Bureau's belief that it should use financial institutions as an arm of the law to regulate auto dealers.

Mr. WILLIAMS. There is a thing called reputation that we all deal with. At the end of the day, that is all we go home with is our reputation with our customer, something the Federal Government does not understand. So thank you for your testimony.

My next question is to Ms. McGrath.

Last month you wrote an article for the American Banker that indicated that Congress might be inadvertently ignoring the regulation burden on small and mid-sized community-based non-depository mortgage lenders. Would you help me and others understand how and to what degree the non-CFPB regulators audit and oversee your business?

Ms. MCGRATH. Yes. Thank you very much for the question.

Every single one of the non-depositories that is a licensed mortgage lender is being regularly audited by every single State in which we conduct business. So in all of the seven States in which I operate, we have an audit.

In addition to that, we are also audited by the FHA, the VA, and the USDA. My company has recently become Fannie Mae-approved, so soon we will also be audited by Fannie Mae.

All of these States in addition to our warehouse providers. Bear in mind that as a non-depository we have to borrow money in order to lend it to consumers, and so our warehouse providers will also audit us as well and do all sorts of checks to make sure that we have the financial wherewithal and that our policies and procedures are in place.

I would also like to add that in addition to that, just back to the non-depository point, is that all of us that are non-depositories, in order to conduct—in order to close these loans, we usually have to put our own personal guarantees on the line for these transactions. So the thought that we are trying to avoid the ability to repay because we want to do riskier loans is simply not true. I have no de-

sire, and my business partner has no desire, to buy back a loan because we have not done a good check to make sure that the borrower has the ability to repay.

Mr. WILLIAMS. Next question: How does this affect the types of products you might or will offer a customer?

Ms. MCGRATH. At the end of the day, the products are the products that are out there that we are able to sell into the secondary market, so we applaud the ability to do those loans but we have to stay within the QM parameters because we have to be able to sell these loans in the secondary market.

So the bulk of our loans are QM lending. Again, we are small non-depository lenders with good track records who are trying to provide consumers with the loans that they need.

Chairman NEUGEBAUER. The gentleman's time has expired.

Mr. WILLIAMS. I yield back. Thank you.

Chairman NEUGEBAUER. Based on the question from the gentleman from Washington, I just want to let you know that when the yellow light comes on, you have 1 minute remaining. You can look at the lights on the table there.

The Chair now recognizes the gentleman from Massachusetts, Mr. Lynch, for 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman.

I want to thank all the witnesses. I think you have all been very, very helpful, each of you, in helping us grapple with this issue.

But, Ms. Wilson, I wanted to focus on you. I know the comparison was made earlier to alcohol and smoking, I guess, regarding choices that could be made.

And I know that we in the legislature have put limits on those who sell alcohol and we say, "Look, young people are not able to really make that choice so we are going to put a limit." You have to be 18 to buy alcohol.

We also put limits on people buying cigarettes because young people—I remember for years when I was younger during spring break the cigarette companies would be down there in Florida and elsewhere giving free samples of cigarettes out, and young people were unable to—well, I think they were exploited. There was an information asymmetry where they just didn't have the wherewithal, and that circumstances weren't good for them making a decision in that circumstance. So we did away with that pretty much.

I have some areas in my district that are underbanked, including Brockton, Massachusetts. We were hit pretty hard by subprime lenders and there was an informational asymmetry, and also there was—the community is underbanked.

We have convinced some credit unions to go in there and try to help people out, but mortgages were not available so the folks who were selling subprime had a field day down there. And then when the crisis hit, boy, it really hit Brockton very, very badly, and they are just recovering now.

Unlike some of the—I also represent Boston. They are well-banked and it is not a problem.

But for the folks that we are talking about who are exploited by payday lenders, do they really have a choice? Do they really have—is it as simple as that—they can either go to the payday lender or

they have another institution that will lend to them at a better rate?

Ms. WILSON. Representative Lynch, I actually thank you for making those points because I think you bring out an important perspective that takes us back to the title of this hearing and the initial question.

One of the things that the Center for Responsible Lending has been very public and adamant about is the importance of actually making sure that community-based banking institutions have an opportunity to compete. And the reality is because most of the conversation has focused not on actually granting legitimate relief to community bank financial institutions, and instead addressing topics like payday lenders and those other institutions, we haven't been able to do that.

So the reality is that one of the things we would like to see is that this conversation should focus on how do we get credit unions and community banks to offer legitimate alternatives at lower interest rates for consumers in traditionally underserved areas? That is a conversation worth engaging in. That is a conversation that Congress can do great benefit to American consumers for addressing.

But that is a very separate thing than saying that it should be acceptable to charge 300 percent or 400 percent interest rates.

Mr. LYNCH. All right.

I traveled a lot as an iron worker before I came to Congress and oftentimes I would only be in a place maybe 6 months, 8 months, and many times shorter times than that, and you would have to go to a payday lender to cash a check because you didn't have—you are actually sort of a traveling worker, so you wouldn't have a connection to that neighborhood or that city. And so without an established residence, you had to rely on payday lenders. And they typically take 2 percent of your check plus a fee—plus a fat fee.

So, you see where people don't have that—and many can't go to a regular bank. You have to get an account, and you might be leaving there, so to set that all up was just not practical.

So I have seen firsthand how some people can be taken advantage of if they don't have all the advantages that other people might have.

So anyway, I will yield back the balance of my time.

And thank you all for your testimony.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from Missouri, the chairman of our Housing and Insurance Subcommittee, Mr. Luetkemeyer, is recognized for 5 minutes.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

I have a quick question for Ms. Wilson.

Your testimony, apparently, with the RESPA–TILA situation, the TILA–RESPA integration situation, leads me to believe that you are not supportive of the 6-month hold-harmless period. Is that what I will read you—

Ms. WILSON. You mean a delay by the Consumer Financial Protection Bureau—

Mr. LUETKEMEYER. Right.

Ms. WILSON. —in enforcement?

Mr. LUETKEMEYER. Right.

Ms. WILSON. As a general matter, I made that testimony to—

Mr. LUETKEMEYER. Either you are or you aren't. Yes or no?

Ms. WILSON. So what I would say is this: I think that it is perfectly consistent with what the CFPB has done before to allow some delayed enforcement. My point was to suggest that unlike other instances—

Mr. LUETKEMEYER. My point, Ms. Wilson, is that CRL signed a letter 3/18, a trade letter that asked CFPB to consider a hold-harmless period of 6 months. Do you change your position?

Ms. WILSON. It is not a change in position. What I wanted to—

Mr. LUETKEMEYER. Okay. So you agree with the chairman and I in our position, and agree with the industry to try and have a hold-harmless period here where we can sort of find a way to make this thing all work. You agree with that, then, I take it. Yes or no?

Ms. WILSON. That is easy. Yes.

Mr. LUETKEMEYER. Okay. Thank you very much.

Ms. McGrath and Ms. Evans, along that same line, I am just kind of curious, before CFPB came out with their rules, were your industries, your associations working with CFPB at all to try and help form some rules and regulations that would actually be workable? Were you working with—were they working with you?

Ms. MCGRATH. Excuse me. Thank you for the question.

We have certainly reached out to them through our organization and tried to start a dialogue and tried to become involved in the process, but for the most part we were told that we just would have to wait until it came out.

Mr. LUETKEMEYER. Okay.

Ms. Evans?

Ms. EVANS. Thank you for asking the question. Yes, most certainly, we were very actively engaged in the comment period when the proposed rules were put forward. And actually, the CFPB did consider many of our comments.

But the remaining outstanding issues are critical to the—to actually the goal of the CFPB to make sure consumers are better informed.

Mr. LUETKEMEYER. Ms. Evans, I think you were the one who made mention of the fact that you were—you had some—or maybe it was—I think it was you—made mention of the fact that you had an issuance of best practices. Did CFPB put any of those into place in their regulation?

Ms. EVANS. No, sir. They did not. In fact, the best practices standards that we put forward were in response of the lack of direction that the CFPB has not done.

Thank you

Mr. LUETKEMEYER. Thank you. Thank you very much.

Mr. Shaul, I am kind of curious—I am someone who is sort of very involved in the Operation Choke Point discussions and trying to push back the DOJ and the FDIC with their actions, and I know that payday lending is in the crosshairs of Operation Choke Point.

So I am sure at this point all the different storefronts and individual businesses that have been affected by this, can you—there is bound to be some sort of access to credit problem that we have

gotten. Can you determine, give us an idea of just how much it has affected the access to credit by Choke Point actions?

Mr. SHAUL. It has affected access to credit indirectly and directly. Some smaller entities have been forced out of business, notably in States like California.

It is also true that entities across the country have borne increased costs because the issue here is not one that is commonly understood. It goes to the ability to bank proceeds on a daily basis in banks that are close to the institutions. So many members, for example, have had to hire armored trucks to take cash from point to point.

The beauty of this, from our point of view—or the irony of it—is at the same time that this is occurring to our members and to others, the Justice Department has struggled to find a way to put marijuana proceeds in banks. It is curious that we are State-licensed, in business for more than 15 years, and constitute, in my judgment, little if any reputational risk to a bank, and yet our position is inferior to that of a marijuana—

Mr. LUETKEMEYER. I have one quick question. I see the yellow light has come up on me.

With regards to CFPB's new rulings that have come out with regards to payday lending, how much did they study this? Are you aware of the length and breadth of the studies that they did before they issued these rules or did they do it at all?

Mr. SHAUL. I am not fully aware—they say they have been at this for 3 years, but our judgment is that there are two problems: they have not asked the proper questions in regard to research; and their research is incomplete.

For example, in SBREFA they have not done product-by-product research. They have not done research that is on small entities, even though SBREFA is meant to address small entities as a proposition.

Mr. LUETKEMEYER. Thank you very much.

Thank you, Mr. Chairman.

Chairman NEUGEBAUER. I thank the gentleman.

The gentlewoman from California, Ms. Waters, the ranking member of the full Financial Services Committee, is recognized for 5 minutes.

Ms. WATERS. Thank you very much.

For full disclosure, I am very supportive of the Consumer Financial Protection Bureau. I think Mr. Cordray has done a wonderful job. I served on the conference committee for Dodd-Frank reform, and I made sure that I did everything that I could to make sure that the CFPB was—became a part of the reforms that we were doing.

For further disclosure, Ms. Wilson was asked a lot of things. She was asked whether or not she liked the CFPB, I believe. She was asked about smoking. She was asked about liquor. She was asked about a lot of stuff. Let me be clear—I think she was asked about payday loans, not the CFPB.

And you weren't given a chance to answer many of the questions that were put to you because you have been interrupted by Mr. Luetkemeyer, Mr. Pearce, and Mr. Neugebauer here today. But let

me just say, even though you haven't had a chance to say it, I don't like payday loans. So I want everybody to be clear about that.

Let me ask you, Ms. Wilson, you said some banks and credit unions make loans at rates much less than 28 percent. Are these charity loans or can short-term loans be profitable and affordable?

Ms. WILSON. Congresswoman Waters, thank you for asking me that question, because the reality in the experience of Self-Help, CRL's affiliate, is that they are profitable. And it is not charity; we are in business to make money.

And our experience is that you can make short-term loans to consumers who are of low- and moderate-income backgrounds, or in minority neighborhoods, and they can be profitable and successful. The key is to actually make sure that they have an ability to repay that loan and that the loan is designed in a way where they can actually meet the terms.

So no, they are profitable, and yes, we are in the business of making money.

Ms. WATERS. Thank you.

Let me ask our gentleman here today who is representing payday loans—I think it is Mr. Shaul—there has been a lot of criticism about the 400 percent interest, 455 I think Mr. Clay said. You have been criticized about the cost of your loans.

Why do you charge 400 to 455 percent for your loans? Why do you do that?

Mr. SHAUL. Ms. Waters, it actually stems from the fact that it is necessary as a proposition to stay in business to have a larger interest rate for a short-term loan, especially if it is in conjunction with a storefront—less from the standpoint of the number of defaults, more from the underlying cost of servicing those loans.

Ms. WATERS. I understand that it—I believe you get capital from some of the larger banks. For example, you are able to obtain capital to run your businesses and to make loans, et cetera, from some of the larger banks. Is that right?

Mr. SHAUL. I think that would be a minority point of view. I do not think that is—

Ms. WATERS. You have not received capital from Chase Bank?

Mr. SHAUL. I do not believe that Chase Bank is supplying lines of credit to anyone in our industry—in our—

Ms. WATERS. What is the cost of your capital—the money that you get from wherever you get it from?

Mr. SHAUL. I'm sorry, I missed the question.

Ms. WATERS. The capital that you use to make loans with, to run your business with—I don't know where you get it from, but what does it cost you?

Mr. SHAUL. It would vary from institution to institution. Some is through private placements; some is through partnerships and so forth. So I could not give you a complete answer to that.

What I could tell you is that our return on capital is less than banks' return—large banks' return.

Ms. WATERS. Thank you.

Let me just say something about the automobile industry here. There are a lot of people who are watching what is happening in the industry, and we find that we are afraid that what happened

in the housing market with subprime lending is now what is happening with automobile lending, and we are worried about that.

We see people—and I know people, and I have constituents even who are walking into these automobile places and they are getting cars without their credit being vetted, but they are paying 40 percent interest on the loans that they are getting. What is going on and why is this happening?

Mr. Friedman, I am speaking to you.

Chairman NEUGEBAUER. The time of the gentlewoman has expired.

Ms. WATERS. Would you allow Mr. Friedman to answer the question, Mr. Neugebauer?

Chairman NEUGEBAUER. Briefly.

Mr. FRIEDMAN. Ma'am, as far as the rates that you are talking about, I wonder if you are referring to buy-here-pay-here dealers, which is not the industry that I represent. We represent indirect auto lenders, captive finance companies, independent finance companies, and banks that offer credit that is transacted by dealers to purchasers of new and used automobiles.

Ms. WATERS. I am talking about the industries you represent, yes.

Chairman NEUGEBAUER. I hate to do this, but we are going to have to vote here in a little bit and I would like to get as many Members in as possible, so I am going to have to—if you want to get one of your staff members to reach out to the Member to answer that question.

I am now going to recognize the gentleman from Pennsylvania, Mr. Fitzpatrick, for 5 minutes.

Mr. FITZPATRICK. I thank the chairman for calling the hearing. This is a really important subject, and I have found the testimony of all the witnesses to be really helpful.

I keep in close contact with my constituents back in Bucks County, Pennsylvania, those who represent consumers and represent buyers and sellers at the real estate settlement table—lenders, title agents. And, you know, while I think we all can agree that consolidation of all these procedures and all the forms, all of which were designed to help consumers and that is good, but the consolidation is a good thing.

As was pointed out by Ms. Evans, we are 107 days away from implementation, and as hard as they are trying—buying software, trying to coordinate things—they are concerned about that hard-and-fast deadline. And so I want to associate myself with the letter that Chairman Neugebauer and Chairman Luetkemeyer have written to the CFPB asking for a responsible, reasonable deferral so that everybody can sort of get things in order.

I asked some of my constituents what their concerns were specifically, in preparing for the hearing today, and one particular constituent was talking about the Real Estate Settlement Procedures Act, I guess the HUD–1 settlement form. And he wrote that the new closing disclosure set to go into effect as of August 1, 2015, has to be delivered to purchasers 3 days prior to closing receipt. Receipt has to be confirmed via email or certified mail or hand delivery, and no changes can happen once received.

Is that an accurate recitation of what we are looking at as of August 1st?

Ms. Evans or Ms. McGrath?

Ms. MCGRATH. Yes, absolutely. That is very true and it is going to be incredibly cumbersome.

And one of the concerns that we didn't really talk about during this hearing is that when you think about the multiple transactions that can sometimes go back to back with different sales of homes, a delay in any one of those transactions in the chain will cause a delay in all of them. So it could be devastating.

Mr. FITZPATRICK. Ms. Evans, I assume you have done thousands of real estate settlements?

Ms. EVANS. Yes, you are exactly right.

And the bigger issue is the rule is so specific that even email delivery isn't acceptable; it has to be—meet an esign standard that for the most part most consumers aren't familiar with, so it requires the extra burden of educating the consumer about what deems acceptance.

Mr. FITZPATRICK. What happens if a consumer is not represented by a REALTOR® or just literally go into the settlement on their own?

Ms. EVANS. They are subject to the same rules, same obligations—

Mr. FITZPATRICK. Can I just, by show of hands, the panelists—the five panelists here—who have actually represented a buyer or a seller or a lender at the settlement table when these kinds of rules actually have to be implemented? Which of the five of you have represented people—have actually gone to real estate settlement other than for yourselves?

Just the two of you?

So what happens when, 3 days, 2 days before a settlement, there are adjustments? There is oil in the oil tank that needs to be reimbursed, maybe people, families are moving out of a home and maybe there is debris left that somebody needs to remove and pay for.

In my experience, these things are minor adjustments at the settlement table that happen in just about every real estate transaction—they are small but they are important, especially to a buyer who is putting out a lot of money for a home. What happens to those minor adjustments under these new HUD–1 regulations?

Ms. EVANS. Actually, those minor adjustments may cause a delay and a total reset of the transaction, which in most instances does nothing but cause harm to that consumer.

When a consumer approaches closing, they are in—they are wanting to close on that home. They perhaps have the moving van sitting in our parking lot. They may have their children being entertained in our conference rooms. And they are wanting to close the loan, move into their new home so they can get on with their life.

We may have a seller getting ready to take those proceeds and go on and purchase another home, and exactly as Ms. McGrath said, a delay in one transaction will cause tremendous consequence for the subsequent transactions following.

Ms. MCGRATH. And I would add to that, I just want to reiterate something I said in my verbal statement is that this is currently—some of this is in effect now already because of changes in the APR and what can happen, and in many instances, again, it is a change that can—not to the borrower's—it is not going to negatively impact the borrower. It is actually in their benefit.

But because it is a change in the APR we have to re-disclose and the clock has to start ticking again.

Mr. FITZPATRICK. Right. And that causes, yes, other—in my experience of representing real families, including at the settlement table, August 1st is probably the most difficult time because everybody is trying to get the settlement done before the new school year starts. It seems January 1st, if you are going to enact these and put these changes into effect, is a better time.

It is a responsible deferral, still putting the rules into effect, and I would hope that the Center for Responsible Lending would continue to advocate for that reasonable extension.

Thank you, Mr. Chairman.

Chairman NEUGEBAUER. I thank the gentleman.

Another gentleman from Pennsylvania, Mr. Rothfus, is recognized for 5 minutes.

Mr. ROTHFUS. Thank you, Mr. Chairman.

Mr. Friedman, I wanted to ask you about the Charles River Associates report.

During a hearing on March 4th, I questioned Director Cordray about the Charles River Associates study that examined the Bureau's disparate impact methodology for indirect auto lending. I pointed out that the Bureau had yet to publicly acknowledge the study and I questioned the Director on whether he could commit to correcting any errors or bias in the methodology before pursuing any further disparate impact claims under the Equal Credit Opportunity Act.

Unfortunately, the Director could only say that the Bureau had looked at the study. He didn't agree with the conclusions and didn't find any obligation to respond. He also stated that the Bureau was still thinking about the study and what it might mean.

Personally, I think it is pretty troubling that the Bureau was attempting to further expand its unaccountable authority by attempting to regulate businesses that are specifically exempt from Bureau supervision under the Dodd-Frank Act, and I also think it is pretty troubling that Director Cordray couldn't or wouldn't commit to making necessary corrections to fix the methodology in order to improve the accuracy of the Bureau's findings.

I would like to give you the opportunity to respond as well. What do the results of the Charles River Associates study mean for your members?

Mr. FRIEDMAN. Thank you for that question, sir.

I will say that based on the findings of this independent report, when appropriately considering the relevant market complexities and adjusting for a proxy bias and error, the CFPB's observed variations in dealer reserve based on race are largely explained by business factors.

And so for the companies under the CFPB's jurisdiction, they are struggling to get to the bottom of this. The CFPB has alleged dis-

parate impact, which means statistical unintentional discrimination based on neutral lending factors, and these companies want to work with the Bureau, but under the Equal Credit Opportunity Act we don't collect or maintain demographic information on borrowers and proxying is necessary. Unfortunately, the methodology put forward by the Bureau gets it wrong two out of five times.

Mr. ROTHFUS. Two out of five, that is 41 percent.

Mr. FRIEDMAN. That is right, sir.

Mr. ROTHFUS. How do you respond to the fact that the Bureau is attempting to hold vendors liable when their methodology is off by 41 percent?

Mr. FRIEDMAN. I would say that if you are trying to market a product to a particular community then you might be satisfied with guessing their race or ethnicity by a 59 percent accuracy rate, but from a law enforcement perspective, I don't think that is appropriate.

Mr. ROTHFUS. This question is for everybody on the panel. In a hearing last month on regulatory burdens for depository institutions, I spent my time questioning—focusing on problems that come about when you have a one-size-fits-all, Washington-knows-best approach to regulating community banking.

I made the point that this mindset has a direct impact on the ability of financial institutions to serve their local communities, particularly those people in need, and the witnesses discussed the products and services that are no longer offered today, such as free checking. I would like to give you the same opportunity today.

Are there any specific rules or proposals that you believe will have a significantly detrimental impact on access to credit for financially underserved Americans?

Ms. McGrath, we can start with you and go down the line.

Ms. MCGRATH. Thank you very much for the question. I think that the statistics have shown that the regulatory burden on lenders has caused a dramatic decrease in first-time homebuyers, and the numbers are out there and it is very obvious, and you can see it in the sales as well in specific areas. For example, in Houston the sales show that loans under $100,000 have decreased, whereas loans—or, excuse me, home sales under $100,000 have decreased whereas home sales above $500,000 and above have increased dramatically.

So I think that it is important to note that one size does not fit all, because the regulatory burden is a fixed cost on many of these institutions, and the large banks can absolutely shoulder that burden, whereas the smaller lenders—the smaller depositories and non-depositories alike cannot. And that is what is leading to all of the consolidation and the lack of choice.

Mr. ROTHFUS. Mr. Friedman?

Mr. FRIEDMAN. I would just add that I represent consumer finance companies that make personal loans, traditional and installment loans to consumers. And in the past they often would make real estate loans, particularly home equity loans, to good customers, and they have all but exited that marketplace due to just sort of the sum total of the regulatory changes in the mortgage space.

It was an incremental part of their business, but it was an important part to their customers, and now they don't do it anymore, and their consumers find fewer options in that space.

Mr. ROTHFUS. Ms. Evans?

Ms. EVANS. Thank you. The issue with our industry is the fact that the cost of meeting the standard set forth under the new regulation is cost-prohibitive for many of our small members and eliminates competition and choice in our small markets for those consumers who reside in those rural and smaller areas.

Mr. ROTHFUS. I see my time has expired, Mr. Chairman. Thank you.

Chairman NEUGEBAUER. The gentleman's time has expired.

The gentleman from South Carolina, Mr. Mulvaney, is recognized for 5 minutes.

Mr. MULVANEY. Thank you, Mr. Chairman.

I would like to start with Mr. Shaul and ask some general questions about your opening testimony, and then also follow up a little bit on what Mr. Luetkemeyer asked you about the SBREFA process.

You said in your opening testimony that as well-intentioned as you thought Dodd-Frank was and the concept of the CFPB was, it has sort of gotten astray from its original intention. Why do you think that is?

Mr. SHAUL. I think there is a natural tendency in Bureaucracies, whether they are governmental or not, to continue to expand their territory, and in this case I think we all would have been better served if there had been limited objectives for the CFPB and limited problems solved before they launched into areas that are dubious at best. Auto lending is one such area.

I think that their look at our industry ought to be disturbing to everyone who envisions rules being made for them, because the research that they have done in our industry fails to take into account the Federal structure, and it also, I think, fails to take into account what Dodd-Frank really said. What Dodd-Frank really said was that we were to be regulated.

The proposals in front of us don't regulate us; they virtually drive us out of business. And in addition to that, they are saddling us with a set of comparabilities, in terms of other products to be regulated, that make it almost impossible to have a straight dialogue on payday lending.

Mr. MULVANEY. Let me ask you, following up on Mr. Luetkemeyer's comments regarding the outline of proposals under consideration, the alternatives to consider to the March 26th document you mentioned in your opening testimony that I think identifies on—I think it is page 45 specifically—says about 60 percent of the small lenders are going to go out of business, they are going to close. That is the CFPB's own admission that is the impact here.

Did I hear you say that is not the intent of—when you worked on drafting Dodd-Frank and CFPB, that was never the intent of what you worked on?

Mr. SHAUL. No. I don't think that the intent of Dodd-Frank was to annihilate businesses, and I also do not think that there is a full understanding of the consequences—the indirect consequences that follow from the acts that the CFPB will take. And by that, specifi-

cally, I mean that if you look at non-prejudiced research done by the Federal Bank in New York and done in Kansas City, you see consequences that are not readily seen at the moment the prohibition is made or the restriction is made.

So I think the error here is the belief that a relatively inexperienced agency with very little as a track record has the stature to look forward for an industry as a whole and predict what the consequences of its rules will be. A measure of caution, humility, and a greater willingness to have a full discussion would serve the CFPB well.

Mr. MULVANEY. And there is another aspect to it here that I am hearing from back home that we won't have time to explore today, which is one of the ways the CFPB, it strikes me, could get that sort of insight and that fuller understanding of the impact, is to work closely with the industry that they are seeking to regulate or to oversee. But what I am hearing from back home is a perfectly reasonable question, which is, why should we work with somebody who has come out on public record and said they want to put 60 percent of us out of business?

That is a very difficult and adversarial relationship in which to build that type of understanding, but if—given that is the stated purpose, Ms. Wilson, of the CFPB, I will ask you to follow up, as well, on something you said during your opening statement: that consolidation was bad for the consumer, that choice was good for the consumer. Would you agree with me, ma'am, that driving 60 percent of the small lenders in this country out of business is bad for the consumer?

Mr. SHAUL. It is bad for consumers. The closing of cash advance at banks was bad for consumers, even though it is a competitor of ours.

When I am asked questions about rates, the first thing I think people ought to understand is the rate is largely because it is a short-term loan. But the second part of that is it will only become lower as there is real competition—not subsidized competition, not competition that doesn't tell the whole story.

When we get into these questions of other comparables, add the fee, add the byproducts that are included in this and you will see that almost none of the experiments, including Sheila Bair's experiments through the FDIC, to give a counter to payday lending works because they don't turn a profit.

Mr. MULVANEY. Ms. Wilson, let me close with this: Mr. Pearce asked you a question that I think he offered you in a rhetorical fashion, which is, what do you say to that person working in the oil fields in New Mexico who wants to borrow $100 today and pay it back on Friday at $120?

You support, I think, based upon what we have heard today, getting rid of that particular industry. What do you say to that person? It is not a rhetorical question.

What do you say to that person who calls you up on the phone and says, "What gives you the authority to take this choice away from me?" What is your answer?

Chairman NEUGEBAUER. Briefly, please.

Turn your microphone—

Mr. MULVANEY. Brief, but not that quiet.

Ms. WILSON. I'm sorry about that.

So briefly, my answer would be that the law has longstanding recognition of the fact that usurious rates are bad. And so it is not a question of actually taking away the option; it is a question of making sure that the option is actually a legitimate choice.

Mr. MULVANEY. And I will put it to you, Mr. Chairman, that when the law has the effect of hurting individuals, maybe the law should change.

Chairman NEUGEBAUER. I appreciate the gentleman's comments.

Now, Mr. Friedman, I just want you to know I am about to recognize your former boss for 5 minutes of questions, so you might want to fasten your seatbelt.

Mr. FRIEDMAN. Uh-oh.

Chairman NEUGEBAUER. I now recognize the gentleman from California, Mr. Sherman, for 5 minutes.

Mr. SHERMAN. I would point out that there is a lot of usury that isn't called usury. It is when you can't get your car out of the shop and you have to go rent a car or use a bus because you can't get a $400 loan. It is when your lights are turned off, and there is no usury there except it costs $100 to get them turned back on, not to mention what you pay for candles in between.

But that doesn't mean that every payday practice ought to be allowed.

Ms. Wilson, you talk about ability to pay, and I hope that you will help us develop a more sophisticated phraseology of that because in every 100 borrowers there is somebody who isn't going to pay, and I don't want to go back and have a class action lawsuit against the lender.

The only reason they are making the loan is because they know 90 percent of the people are going to repay eventually. Every payday lender would be out of business if nobody—if 20, 30 percent didn't pay him back.

So it really comes down to whether a substantial majority of those borrowing are going to repay substantially according to the terms of the agreement. So the one problem—the character of payday lending is yes, people repay, but the original agreement is they are borrowing the money for 2 weeks and they end up paying back 26 weeks later.

So I hope we can work with a more sophisticated standard that would look in terms of does a substantial majority of the borrowers repay with only a few late fees or a few extensions?

If we were to say that a substantial majority had to repay a loan without any deviation from the terms of the loan, I couldn't get a mortgage. I had a late payment. Everybody I know had a late payment once.

So I guess the point I am making is it can't be ability to repay eventually, and it can't be ability to repay exactly according to the terms with no late payments. It has to be a way of looking at the—what loans are being made and whether the majority can substantially comply with the loan agreement.

I think this question has come up a bit, but the issue is whether we should have a commission rather than a single commissioner over at the consumer protection agency. When you have just one commissioner it is of the President's party, and so I strongly be-

lieve in having one commissioner right until the end of 2016. But I don't know who the President is going to be in 2017, and neither do the gentlemen over there, so this might be a good time to be bipartisan effective 2017, which has a 50 percent chance of being adverse to one of the other of us.

Chairman NEUGEBAUER. Is that an offer?

Mr. SHERMAN. That is an offer.

Chairman NEUGEBAUER. We will talk—

Mr. SHERMAN. I will start with Justin because I promised to torture him a little bit, but—and also anybody else—what are the advantages and disadvantages of going with a commission rather than a commissioner, knowing that a commissioner is a little cheaper—a tiny bit cheaper and a little bit faster?

Justin?

Mr. FRIEDMAN. As I discussed with Mr. Scott earlier, I think that a multimember commission provides a process by which issues are considered carefully and staff has to make a case to the commission before they go forward with a rule or an enforcement action, and it is a more deliberative process that produces better policy that offsets consumer protections against the need to ensure affordable access to credit.

Mr. SHAUL. May I—

Mr. SHERMAN. Yes. Go on—

Mr. SHAUL. Let me give you an example. When the CFPB presented its paper on where they intended to go with short-term, small-dollar lending, essentially a payday story and a media event, it was entitled, "Debt Traps."

If you had a commission, I believe that there would have been a dissent, which would go along these lines: Before you say "debt trap," prove it. Before you say, "debt trap," remember that you are the arbiter and you are giving the sense that you are not partisan.

Mr. SHERMAN. I get it. And I would like to propose that for this committee instead of having a chairman we have a commission decide, because I have seen titles of hearings such as, "Examining the Regulatory Burdens But Not Any Benefits to the Consumer on Non-Depository Financial Institutions." So the title of the hearing can be very important, and the desirability of a commission to make all decisions is duly noted.

Chairman NEUGEBAUER. Maybe we can discuss that in 2017, as well.

I now recognize the gentleman from Colorado, Mr. Tipton, for 5 minutes.

Mr. TIPTON. Thank you, Mr. Chairman.

And thank you, panel, for taking time to be here. I would like to start with Mr. Friedman.

Your members include credit card issuers that make credit available to consumers, which is especially important to the 68 million underbanked consumers in the United States, including those in my district. The CFPB released an 870-page proposed rule to regulate those prepaid card products, and my constituents have reached out to both myself and the CFPB to let it be known that they are not in favor of this proposal.

As comments from customers in Grand Junction to Montrose to Pueblo, in my district, my constituents want the opportunity to

have overdraft protection on their prepaid cards. How do you believe the CFPB's proposal on prepaid cards will impact the ability of the underbanked to access these important features like overdraft protection?

Mr. FRIEDMAN. Traditional installment lenders don't generally offer stored value cards. That is something that they are looking at in the future as technology changes and consumers are demanding cards instead of cash or checks or deposits. They are popular among the underbanked community, and there is certainly a lot of very interesting innovation going on in issuing general use prepaid cards.

As far as the CFPB's proposal, we would just say that we hope that the government won't stand in the way of lenders using stored value cards to make loans and to extend credit to consumers.

Mr. TIPTON. Just for the point of clarity, overdraft—you opt in, you are not forced. Is that correct?

Mr. FRIEDMAN. I am less familiar with this rule since our members generally don't—

Mr. TIPTON. I believe that is pretty accurate. It is something that you have the choice to be able to do.

And I see Mr. Shaul nodding his head—

Mr. SHAUL. That is right, I believe, yes.

Mr. TIPTON. It is. It is in opt-in fashion, so if we keep the government out of the way we are going to be able to help underbanked people actually have access to credit. Thanks.

I would like to follow up—and by the way, it is great to see a fellow Coloradan here in Ms. Evans.

Several things in your written testimony did catch my eye, and it is basically to the title of this hearing, "Examining Regulatory Burdens on Non-Depository Financial Institutions."

You cited an example in your written testimony, and it was a Nancy McNealy, a small business owner, small real estate title company. Because of regulatory compliance under TRID, she is seeing a 5 percent increase in the cost of her business. No increased revenue coming in, but because of government regulation, an additional 5 percent in cost.

Is this a common pattern that we are seeing as regulations continue to compound out of this Administration?

Ms. EVANS. Absolutely. Our industry is a highly regulated industry at the State level, which is where real estate transactions take place, in local markets. And for a Federal regulator to create a one-size-fits-all burden on our businesses across the Nation, large or small, we are facing huge financial costs in order to implement those standards.

Mr. TIPTON. Huge financial costs. You just described a tier of regulatory requirements at the State level, now a compounded tier of regulatory requirements—and they aren't all still written yet, by the way; they are still to come—coming out of the Federal Government.

I assume in your position and others on the panel, all of your businesses are so profitable that you can afford whatever costs that the government wants to pile onto you. Is that accurate?

Ms. EVANS. No, sir. Not at all.

Mr. TIPTON. It is not. It is not accurate that you can continue—who is going to ultimately pay those costs? Do you have to pass those on?

Ms. EVANS. Ultimately, if you were going to remain profitable, yes. That consumer—

Mr. TIPTON. You are going to pass those on.

In your written testimony, you cited a young family just getting started with a child on the way, Brianna and Emina were their names. Here were their comments: Throughout the process, because of regulatory requirements they had on their loan, the couple was frustrated because they continually had to resubmit, resign, and re-date every line. Every request was repetitive and last-minute.

How is this helping the consumer?

Ms. EVANS. It is not.

Mr. TIPTON. It is not helping the consumer. So the Federal Government saying it is here to help has become a hindrance.

Ms. EVANS. That is correct.

Mr. TIPTON. That is correct.

So are you challenged like I am—and maybe, Ms. McGrath, you have had some experience with this. When I think of a young family, Brian and Emina, with a child on the way, they are trying to get this structured so that they would be able to be in the home, as the chairman had noted in his first comments, trying to close before August, get that family set and to be able to move.

Does this kind of break your heart like it does mine? That we are seeing the government saying, "You can afford to pay more. We will take more out of your pocket because we need another regulation," when we apparently have a system that has worked pretty well?

Ms. MCGRATH. No, absolutely. Thank you for the question. I think you are absolutely right.

The ones who are being hurt the most are those who have less to work with, there is no doubt, and also those who perhaps don't necessarily have the experience with home-buying, so the first-time homebuyer, in particular.

They may not be technologically savvy in some instances. They may not have—how are we going to get these disclosures to them? Some of them don't have email.

How exactly are we going to tell them, "You have to take a day off work so that you can come in and physically sign this disclosure 3 days in advance so that we have proof that you read it and signed it?"

Chairman NEUGEBAUER. The time of the gentleman has expired.

And now the gentleman from Kentucky, Mr. Barr, is recognized for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman.

Mr. Shaul, I was impressed with your testimony, given your background working on the Dodd-Frank Act and describing what was the original intent of the law, certainly not to annihilate businesses—maybe to regulate businesses, but not annihilate businesses such as the industry that you represent.

I represent constituent businesses that are members of your organization, and I have one payday lending business that told me

if these rules go into effect—they are a small two-store outfit—they will, in fact, go out of business. And so that corroborates that anecdotal response, corroborates the estimates of a large portion of the industry just simply going away.

So my question to you is this: What do you expect will happen to customers of those businesses who will no longer be able to access the payday lending option? What other options will they have and what will happen to those consumers?

Mr. SHAUL. Thank you for the question. The first thing that research shows that happens is a rise in the number of bounced checks. It is a fee and it is, in fact, a kind of loan, and it is a way by which people can access credit, but it is a costly way to access credit.

The second thing that happens is many people find themselves going online. If they go online to an established, reputable lender, they will not have a problem.

But our hope with the CFPB, as business people, was that the CFPB would spend particular time on those entities offshore that are nonregulated, unlicensed, unscrupulous, and don't meet a moral standard. That has not fully occurred.

Mr. BARR. So, Mr. Shaul, that doesn't sound like consumer protection to me.

Let me ask you this question: Do you believe that most of the complaints about the payday lending industry—do they come from the customers of payday lenders or do they typically come from consumer advocates who feel that these borrowers are taking advantage of an—I would note in the back of your testimony some of the testimonials from customers—very satisfied customers—of payday loans.

Mr. SHAUL. The customer complaint, whether it is through the portal at CFPB or through the States or through the FTC, is minimal on payday lending, far below that of other institutions.

Now, part of the problem here, I truly believe—and I impugn nobody's motives—is the sense that some class of individuals knows better what to do for another class of individuals than they themselves know. That being true, that being a suggestion that is put forward by many consumer advocates, I would submit that they really don't know either the customer or the customer's needs or patterns.

This year we did a Harris Interactive Poll and we were amazed not just that there were very few complaints, but that the number of—women are 60 percent of our customer base—women who carefully planned out their budget for the month and, when necessary, chose payday lending as a lender—as a softener to their accounts going month by month as they might go up or down.

A fact that is commonly misunderstood with payday lending is for 89 percent of our borrowers it is not new debt; it is a transference. The money that comes in goes to pay something that is already owed. So, so much of this criticism really is not well-founded.

Are there portions of the critique that are right? Of course there are. Are there things that we could do better? Of course there are.

But in the main, this is a question of choice. And frankly, I would not be honest with you if I didn't say that what is really at issue here is the CFPB's attempt to credit ration and their attempt

to decide who will be winners and losers in both the depository and non-depository institutions.

Mr. BARR. Thank you. Thank you, sir.

And I don't have much time left so let me just—quickly to Mr. Friedman, has the Bureau presented, to your knowledge, any evidence whatsoever of any particular instances of deliberate discrimination by any auto dealer or any bank in the country?

Mr. FRIEDMAN. No, sir. And I don't expect they will because the CFPB, under statute, doesn't have jurisdiction over auto dealers.

Mr. BARR. I know about the Ally settlement and some others, but have they distributed a single dollar of those settlements to any alleged victim of indirect auto lending discrimination?

Mr. FRIEDMAN. My understanding is that the Bureau collected $80 million in restitution from Ally in December 2013 and zero dollars of that have been distributed.

Mr. BARR. And that is because their methodology can't identify any victims, is that right?

Mr. FRIEDMAN. That is my understanding, yes, sir.

Mr. BARR. Thank you.

I yield back.

Chairman NEUGEBAUER. I thank the gentleman.

The gentleman from New Hampshire, Mr. Guinta, is recognized for 5 minutes.

Mr. GUINTA. Thank you, Mr. Chairman. I want to follow up or continue this line of discussion.

Back in March of 2013 the CFPB issued guidance that threatens to eliminate auto dealers' flexibility to discount the interest rate that is offered to consumers to finance vehicle purchases. And the guidance offered attempts, I think, to alter the $905 billion loan market, and I think it restricts market competition. I would add the term "credit rationing" that you utilized.

This guidance, in my view, attempts to pressure indirect auto lenders into changing the way that they compensate the dealers to a flat fee system where dealers would no longer be able to discount for their consumers. I see this as a significant problem. I think that this would directly affect the dealer's ability to negotiate with the consumers to help beat a competitor's financing rates, and I think it would also negatively impact the consumer's ability to negotiate a reasonable and what they deem to be an appropriate deal.

Last year the CFPB admitted that they did not study the impact of their guidance and what it had on consumers, so my question is along the same lines to Mr. Friedman.

First—and I think it has been said before but I want to clarify it again for the record—has the CFPB offered a public comment period in regards to this guidance, to your knowledge?

Mr. FRIEDMAN. No, they have not.

Mr. GUINTA. So they have said that auto lending policies may be discriminatory, yet there have been 12 letters from Congress requesting information on this, the CFPB has refused to release any information that would, in my view, help them avoid potential liability by altering their lending—yes?

Mr. FRIEDMAN. Sir, in response to some of those letters, the CFPB did actually issue a White Paper in September 2014 detailing their methodology for proxying for race, and what that paper

revealed is that the CFPB, by their own admission, gets it wrong 21 percent of the time. The analysis that we have talked about earlier from Charles River Associates actually pegs that at a 41 percent error rate.

Mr. GUINTA. Why is there a disparity between Charles River and what CFPB says in terms of the percentage?

Mr. FRIEDMAN. In the Charles River analysis of all aspects of this issue, I think that they have taken a more robust statistical approach than the CFPB does and included other factors at play. The Charles River analysis measures the proxy method against HMDA data, so this is mortgage data where we actually do know the actual race of the borrower. And so what they have found is that the CFPB's method guesses the borrower's race wrong two out of five times.

Mr. GUINTA. Okay. What do you think about the flat fee compensation arrangement preferred by the Bureau? Do you think it would lower interest rates? Do you think it would increase them? And what do you think the impact would be to the consumer?

Mr. FRIEDMAN. Alternative compensation structures such as flats for nondiscretionary dealer compensation may lead to increased borrowing costs for many minority and non-minority customers, and in turn, may limit access to credit for some or all consumers, which is, I think, not a desirable outcome.

Mr. GUINTA. So it is rationing.

Mr. FRIEDMAN. I would say that it is unintentional rationing, but it—that is what we believe would be the result.

Mr. GUINTA. I believe Senator Warren, either last night or this morning, came out with comments already opposing what we are trying to do here, which is again, in my view, to provide flexibility to the consumer and give the auto dealer the opportunity to be competitive, which, quite honestly, last I checked that is what our economic system is built upon is the competitiveness.

Ms. Wilson, I was interested if you had any comments or thoughts about that access to credit, because I know you have talked a little bit about this over the course of the hearing.

Ms. WILSON. Briefly, what I would say is that I understand that people have talked about this question of indirect auto lending as a question of providing discounts. What I would remind you is that discounts that are based on race, religion, or nationality are not discounts; they are discrimination, and it is illegal.

And so the issue that we want to make sure we are talking about in this conversation is whether or not we are engaging in practices that have that correlation to those prohibited categories. And you don't just need the CFPB's analysis to justify that concern in this industry. There are a litany of cases that have been settled—not just Ally Bank, but Namco, Union Bank—

Mr. GUINTA. So would a veteran applying—getting a $500 discount, would that be discriminatory?

Ms. WILSON. What I am suggesting is that if I gave you a $500 discount because you happen to be African-American, that is discriminatory under our law. If I gave it to you because you are White, that is discriminatory. The question is whether or not these practices actually lend themselves to that, and the evidence suggests that they have.

Chairman NEUGEBAUER. The time of the gentleman has expired.

I now recognize the gentleman from—

Mr. SHERMAN. Mr. Chairman?

Chairman NEUGEBAUER. —California for a unanimous consent request.

Mr. SHERMAN. Thank you. I ask unanimous consent to add to the record the statement of the African American Credit Union Coalition, the statement of the National Council of La Raza, and the statement of the Consumer Federation of America.

Chairman NEUGEBAUER. Without objection, it is so ordered.

I also, without objection, would like to submit the statement of the Community Home Lenders Association for the record.

Without objection, it is so ordered.

The Chair now recognizes the gentlewoman from Utah, Mrs. Love, for 5 minutes.

Mrs. LOVE. Thank you.

Thank you, all of you, for being here today.

I just wanted to try and ask these as quickly as I possibly can.

Mr. Shaul, in your testimony about the CFPB replacing State law with their upcoming payday regulation, I just want you to know that concerns me quite a bit because in the State of Utah we have passed a law that actually regulates the payday industry in a responsible manner. As a mayor, I have realized that the most efficient way of dealing with things, the best solutions are found at the most local level.

There are some things that we need to handle on a Federal level, but our legislature crafted legislation that protects consumers but keeps alive this source of credit.

Now, as I understand it, if the CFPB pushes ahead with the rulemaking it will wipe the common-sense law of Utah—it would wipe it out pretty much and replace it with Federal law. Is that correct?

Mr. SHAUL. Yes, Congresswoman, it is correct. And I take particular pride in the fact that I was out there last year when the State legislature in Utah considered this, and I considered the law to be an example of the failure of the Bureau to critically examine what is already happening at the State level. Under the Utah law, which went into effect in January, if a person after three rollovers is—three times asking to continue the loan—does that very act, then at the fourth instance he or she must either pay the loan off in total or go into an extended pay plan, which ends his interest payment and allows him to pay the principal off on time.

This structure we recommended to the Bureau as one they ought to look at if they were genuinely concerned about the issue of how long people were in loans. And so far as I know, it has not been looked at by—

Mrs. LOVE. It is really interesting because as a mayor a lot of times we took a lot of the rules and learned from a lot of the mistakes of other cities and figured out what works. And what I like about that is other States can do certain things and we as a State can look at it and say, "Actually that works," or, "That doesn't work," instead of taking one entity and suffering the consequences of some of those things.

Short-term small-dollar lending has historically been a State-regulated industry, and my understanding is that, in fact, some States have actually banned the practice.

Mr. SHAUL. Correct.

Mrs. LOVE. So do you—do we have any States that do not have the same authority to regulate the payday loan industry? Are there any States that do not have the authority to regulate the payday—

Mr. SHAUL. No. No. Any State can do that. And I must remind you of a statement that was made in an academic forum a year ago in Philadelphia—about 18 months ago, actually, in Philadelphia, in which a panelist who had done research on payday lending said, "Every State has payday lending, but some States fail to recognize that it is going on despite the fact that it is not authorized or registered in their district."

In other words, if you go on in New York State, which bans payday lending, and you look under the payday loans, you will find several ways to get a payday loan. The fact is that people—there is a demand for this product.

Now, if it is brought in every State into daylight and competition ensures, the rates will fall.

Mrs. LOVE. Okay.

I have just a little bit of time and I want to—I really want to get a point across. This, frankly, is not about you or your business. It is not about the banking industry. It is about creating as many products out there.

I remember—I am going to keep the last name out of it because I am trying to protect this person's identity—a good friend of mine coming to me and talking to me about a story where she came home, Maria, I am going to leave her last name out of it, a single mother with three children, came home in the evening and realized that her babysitter said, "You know, I don't have enough milk for the baby." And she didn't have any cash, didn't have any way of getting cash at that time, so she went to her local place and hurried up and that is what she thought about, grabbed milk for her baby and went out and was able to do that.

Had she planned ahead of time would she have done something differently? Maybe, if she had had that time to plan. But it was just another option for her.

Now, this is not—again, it is not about you; it is about people.

I want to say, Ms. Wilson, I appreciate your testimony here today. I want to congratulate you on your award, being named the Woman of Influence by HousingWire Magazine. I think it is absolutely commendable.

But I just want to say, as you go on and you think about some of these things, we really want to get to the same place, which is giving as many people as many options as possible. And we can't forget about the Marias, that if this option didn't exist she wouldn't have that option out there. We cannot pick winners and losers.

And so I want to commend you for what you are trying to do, and I want you to keep that in mind, that we want to give as many options to people as possible.

Thank you.

Chairman NEUGEBAUER. The time of the gentlewoman has expired.

The gentleman from Oklahoma, Mr. Lucas, the vice chairman of the Science Committee, is recognized.

Mr. LUCAS. Absolutely, Mr. Chairman. Thank you very much, sir.

I sense that at least on this end of the aisle and maybe the whole process, I am sort of batting cleanup here.

I would like to go back to the core issues, I think, here and address this to Ms. McGrath and Ms. Evans, because everything has a cost, and for all the discussions we can have about social policy or goals or intentions or a lack of intentions, nonetheless, it is what the real effect is. How many hours would you estimate that your institution has spent trying to comply with the new most recently issued regulations?

Ms. MCGRATH. Oh, goodness. I don't know that we have calculated the manhours, but I can tell you that our association has calculated the cost to its members, and we have seen a 200 percent increase in the cost of compliance from 2010 to 2014 in trying to deal with the regulatory burden.

I can tell you that just in looking at the number of employees, the average company has gone from having two compliance personnel to having seven compliance personnel, so if you look at it in terms of personhours, in that regard, it is astronomical.

Mr. LUCAS. Ms. Evans?

Ms. EVANS. Thank you, Congressman Lucas. Actually, the exact same thing.

I can't tell you the dollar amount, but I can tell you that our organization has had to create an additional compliance division or group of individuals who are focusing totally on how does our IT system work? What new softwares do we need to put in place? What additional training do we need to put in place for our individual employees? And most importantly, how are we getting out there and educating our customers, making sure consumers understand the consequence of this rule, making sure that REALTORS® and lenders understand the consequence of the rule?

It is an astronomical number, and I don't know how to quantify it at this time.

Mr. LUCAS. And I would assume in addition to the permanent personnel brought onboard, probably you have spent a little money on outside consultants trying to work through these issues. Is that a fair assessment, in your home offices and in your parts of the industry?

Ms. MCGRATH. Yes, absolutely. We now hire at least two or three different firms to help us with compliance matters.

And part of that has to do with not being able to get a straight answer out of the CFPB on some of the regulations that they have—that they are trying to regulate. I can't get a straight answer.

Ms. EVANS. And when I look at the consequences to many of our small title providers across the Nation, even in your home State of Oklahoma, and the cost to bring in an outside provider, even the ability to find one in their local market so that the cost is more appropriate and reasonable, it actually could cause significant harm and the inability for that provider to continue to offer services in their market.

Mr. LUCAS. Absolutely. So clearly there is a quantifiable amount there. Clearly, ultimately the consumer is the recipient, because that has to be passed down. That is just the nature of everything.

Like so many things Congress does, whatever the good intent may have been, there is the absolute impact and effect, and ultimately the person we are trying to help pays the price, which is reminiscent many times of the comments in my town hall meetings: "Please stop helping us, Congressman."

With that, Mr. Chairman, I think we have observed how hard this process has helped the American consumer. Let's try to stop helping them while they are still able to survive.

Chairman NEUGEBAUER. I thank the gentleman.

I am going to recognize the gentleman from Georgia, Mr. Scott, for a brief question.

Mr. SCOTT. Very brief question to you, Mr. Friedman. I am a strong supporter of the CFPB, but we have been getting a few concerns. One concern is whether or not we believe that the CFPB understands the differences between banks and the consumer finance companies and the need for the typically unbanked consumer who is served by finance companies.

How do you feel about that, very quickly?

Mr. FRIEDMAN. I would observe that the CFPB's personnel are drawn largely from the ranks of the Federal banking agencies. Generally, historically speaking, States licensed and regulated consumer finance companies, non-depository institutions, and the Federal Government, in conjunction with States, was responsible for depository institutions.

So it just stands to reason that folks who have been dealing with banks and regulating banks for their careers and suddenly have jurisdiction over non-banks will find that it is new ground, and we believe the CFPB would benefit from drawing some expertise from State agencies that have had jurisdiction over non-bank consumer financial institutions for decades.

Mr. SCOTT. So you believe there is some difficulty in the CFPB understanding that, is that correct?

Mr. FRIEDMAN. I do, and I would add that non-banks are more likely to serve unbanked consumers by nature, and these consumers tend to have different needs than banked consumers, and they tend to be more inclined to go to storefront lenders like traditional installment lenders to take out $500, $1,000, or $5,000 and repay it in installments.

Mr. SCOTT. Thank you very much.

Chairman NEUGEBAUER. I thank the gentleman.

Mr. SCOTT. Thank you, Mr. Chairman. I appreciate it.

Chairman NEUGEBAUER. I want to thank the witnesses.

Your testimony has been very informative, it has been articulate, and I think we have all benefited from the comments that have been made today.

I want to thank the folks on my side of the aisle. I think we had all of our Republican Members except for one participate today.

And I appreciate the participation from the Minority, as well.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legis-

lative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And with that, this hearing is adjourned.

[Whereupon, at 3:29 p.m., the hearing was adjourned.]

# A P P E N D I X

April 15, 2015

# OPENING REMARKS

## FINANCIAL SERVICES SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

## "EXAMINING REGULATORY BURDENS ON NON-DEPOSITORY FINANCIAL INSTITUTIONS"

## APRIL 15, 2015

## 1 PM

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THANK YOU, CHAIRMAN AND RANKING MEMBER FOR HOLDING THIS HEARING THIS AFTERNOON. I WOULD ALSO LIKE TO THANK THE DISTINGUISHED PANEL MEMBERS FOR SHARING THEIR INSIGHTS.

IN THE LEAD UP TO THE FINANCIAL CRISIS WE SAW AN ENVIRONMENT WHERE EASY CREDIT WAS ABUNDANT AND READILY AVAILABLE. CERTAIN SMALL DOLLAR LENDERS AND NONBANK FINANCIAL INSTITUTIONS THRIVED IN THIS ENVIRONMENT LARGELY UNREGULATED.

BECAUSE OF THIS LACK OF OVERSIGHT MANY AMERICAN FAMILIES WERE LURED INTO DEBT TRAPS AND LOANS THAT THEY SIMPLY WERE NOT ABLE TO REPAY. IN THE AFTERMATH OF THE CRISIS, WE SAW A LARGE REDUCTION IN CREDIT FROM BANKS, AND CREDIT UNIONS. DESPITE THIS DROUGHT IN CREDIT, NONBANK FINANCIAL INSTITUTIONS THRIVED. MANY AMERICANS WERE LURED BY THE PROMISE OF A QUICK LOAN BY THESE INSTITUTIONS CHARGING EXORBITANT INTEREST RATES AND FEES. AMERICAN FAMILIES SOON FOUND THEMSELVES MIRED IN DEBT TRAPS AND EXTREMELY HIGH INTEREST LOANS. COLLECTION PRACTICES WERE ALSO INVASIVE AND DRACONIAN.

IN MY DISTRICT, PAY DAY LENDERS ARE MORE ABUNDANT THAN STARBUCKS. I HAVE SEEN SOME OF THE CONTRACTS OFFERED TO CUSTOMERS. MANY OF THEM INCLUDE INTEREST RATES ABOVE 400 PERCENT. THAT IS UNCONSCIONABLE.

**FOR THESE REASONS, I SUPPORT THE CFPB'S EFFORTS TO SHED LIGHT ON THIS INDUSTRY AND ON SOME OF THE DECEPTIVE, HARMFUL PRACTICES THAT WE HAVE SEEN. I BELIEVE CFPB'S NEW RULES FOR PAY DAY LENDING, QUALIFIED MORTGAGE RULES, AND THEIR SUPERVISION OF INDIRECT AUTO LENDING WILL PROVIDE MUCH-NEEDED CONSUMER PROTECTIONS FOR MANY AMERICAN FAMILIES GOING FORWARD.**

**MY FIRST QUESTION IS FOR MS. WILSON:**

**→ IN CRL'S ANALYSIS OF CFPB'S PROPOSED RULES FOR PAY DAY LENDING, YOUR ORGANIZATION DISCUSSED LOAN FLIPPING AND THE DISINCENTIVE FOR MANY PAY DAY LENDERS TO VERIFY AN ABILITY TO REPAY. DO YOU BELIEVE THAT THIS PRACTICE HAS BECOME WIDE SPREAD IN THE INDUSTRY? AND DO YOU THINK CFPB'S PROPOSED RULES ARE OVERLY-BURDENSOME FOR PAY DAY LENDERS?**

**MY SECOND QUESTION IS FOR MS. EVANS:**

**→ IN YOUR PREPARED TESTIMONY, YOU STATE THAT TITLE INSURANCE IS REGULATED AT BOTH THE STATE AND FEDERAL LEVEL BUT A 2007 GAO REPORT SHEDS LIGHT ON THIS REGULATION. THE REPORT STATES:**

**"STATE REGULATORS HAVE NOT COLLECTED THE TYPE OF DATA, PRIMARILY ON TITLE AGENTS' COSTS AND OPERATIONS, NEEDED TO ANALYZE PREMIUM PRICES AND UNDERLYING COSTS. IN ADDITION, THE EFFORTS OF HUD AND STATE INSURANCE REGULATORS TO IDENTIFY INAPPROPRIATE MARKETING AND SALES ACTIVITIES UNDER THE REAL ESTATE SETTLEMENT PROCEDURES ACT, HAVE FACED OBSTACLES, INCLUDING CONSTRAINED RESOURCES"**

**DO YOU BELIEVE THAT ENOUGH IS BEING DONE AT THE STATE LEVEL TO PREVENT ABUSIVE PRACTICES IN THE TITLE INSURANCE INDUSTRY, AND HOW DOES YOUR ORGANIZATION PLAN ON WORKING WITH STATES AND THE FEDERAL GOVERNMENT TO ENSURE THAT CONSUMER ARE PROTECTED FROM POSSIBLE CONFLICTS OF INTEREST AND ARBITRARILY HIGH RATES?**

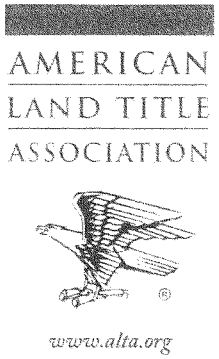
# Examining Regulatory Burdens on Non-Depository Financial Institutions

## House Committee on Financial Services

*Subcommittee on Financial Institutions and Consumer Credit*

***Wednesday, April 15, 2015***
***1:00 p.m.***

***Written Testimony Submitted By Diane Evans NTP, President***



**ALTA President Diane Evans Written Testimony for April 15, 2015**
**House Financial Services Committee - Financial Institutions and Consumer Credit Subcommittee Hearing**

Chairman Neugebauer, Ranking Member Clay and members of the subcommittee, my name is Diane Evans, and I am a vice president at Land Title Guarantee Company, a title insurance agency in Colorado. I joined Land Title Guarantee Company 34 years ago starting as a receptionist. Along with my day job, I have the privilege of serving as president of the American Land Title Association (ALTA).

Founded in 1907, ALTA is the national trade association and voice of the real estate settlement services, abstract and title insurance industry. Our more than 5,500 member companies include title insurers, title agents, independent abstracters, title searchers and real estate attorneys, ranging from small, one-county operations to large national title insurers. The majority of our members are small businesses with the average title agency earning $156,000 in gross annual revenue and employing three or fewer people. Our members employ more than 108,000 professionals and operate in every country in the country where we search, review and insure land titles to financially protect a homebuyer's largest investment and the primary and secondary market mortgage lenders who invest in real estate.

During my tenure as the leader of this organization, I have focused on ensuring our members have the tools they need to comply with the multitude of regulations affecting their business each day. On behalf of all ALTA members, I appreciate the opportunity to appear before you today to discuss the importance of regulatory reform for non-depository institutions.

As Congress considers regulatory reform, it is important to note that title insurance is regulated at the state level and our settlement business is regulated at the federal level. Historically, this dual regulatory structure has been rather complimentary; however, with ever increasing regulation, our members must comply with regulations that overlap and contradict one another. This creates a complex compliance environment and increased costs for our members' businesses, additional liability for our mortgage lender clients and confusion and frustration at the closing table for homebuyers.

As mortgage lenders work to refine their risk management practices to avoid a regulatory misstep, homebuyers and settlement agents are often required to provide documents multiple times signed and dated by the homebuyer. As you can imagine, this process is extremely frustrating and confusing for consumers.

I would like to share an example of how over-regulation impact homebuyers and ALTA members:

> On March 31 a Baltimore couple, Brian and Emina, bought rowhouse in for $245,000. The couple closed on the home right before heading to a hospital for an induced labor for their first child, a boy. Their settlement agent, Nancy McNealy with Consumer Real Estate Title, Inc in Beltsville, Maryland, knew about the labor date and wanted to be sure that she got everything to the lender in a timely fashion so that Brian and Emina could

close and then go to the hospital to give birth. The settlement agent was able to get all of the closing documents together in time. Then, after closing, the settlement agent received another email from the lender that said that copies of tax returns were needed to be signed in order for the lender to fund the mortgage. Throughout the process of obtaining the loan, the couple was frustrated because they continually had to resubmit and resign and re-date every line—every request was repetitive and last minute.

Nancy, the settlement agent in this story, has been in the business since 1979 and employs one other person. She says, "A good month for us is about 12 closings," and her gross revenue runs right around the $156,000 industry average. Most of Nancy's business is from returning clients with whom she has worked for nearly 30 years – she is actually on her 2nd generation of those clients. Nancy believes that small title companies are important to this industry because she has her client's needs in focus and are willing to spend more time and energy on them. Nancy is hands-on with every transaction and knows her customers personally since she lives in this community and sees them and their families at the grocery store. Nancy says, "My reputation is essential."

My testimony today focuses on two ways that Congress, through regulatory reform, can help improve federal regulation of our industry. First, as our industry prepares to implement the Consumer Financial Protection Bureau's (CFPB or Bureau) TILA-RESPA Integrated Disclosures (TRID) regulation, I will discuss commonsense modifications and clarifications to the regulation. We believe the CFPB should develop and announce a plan to provide implementation support during a restrained enforcement period following the August 1 effective date of the regulation through the end of the year.

Secondly, I urge you to support legislation to help improve the way that the Bureau protects consumers while working with small businesses. Specifically, I ask for your support in passing legislation that would create a permanent Small Business Advisory Board and an advisory opinion process at the CFPB.

**Regulation of Title Insurance**

ALTA members provide two primary services to homebuyers and financial institutions. The first service is the preparation and issuance of title insurance policies protecting both purchasers and mortgagor of real property. Insurance products, including title insurance, are regulated by the states and falls outside of federal regulation as part of the business of insurance. Additionally, title professionals act as third-party settlement agents in real estate and mortgage transactions. This service is subject to federal regulation pursuant to the Real Estate Settlement Procedures Act (RESPA), which is within the jurisdiction of the CFPB.

At the state level, title insurance regulation includes oversight of insurer and agent licensing, product regulation, financial regulation, market regulation and consumer protection. States oversee title insurance pricing through the promulgation of rates or reviewing and approving company rate filings. Most states approach rate regulation by prohibiting excessive, inadequate or unfairly discriminatory prices for title insurance.

At the federal level, when title professionals act as independent third-party settlement agents in real estate transactions, they are regulated by RESPA. This law was designed to protect homebuyers through defining and prohibiting kickbacks and increasing consumer understanding by requiring transparency about all of the costs of homeownership.

**TILA-RESPA-Integrated-Disclosure Forms**

In 1968, Congress passed the Truth in Lending Act (TILA) to "assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit."[1] RESPA was then enacted by Congress six years later.

For nearly 50 years, these laws required lenders and settlement agents to provide consumers with similar but different disclosures at the beginning and end of their mortgage and real estate transactions. However, these laws changed when Congress adopted Section 1032 of the Dodd-Frank Act, which required the CFPB to "propose for public comment rules and model disclosures that combine the disclosures required under the Truth in Lending Act and sections 4 and 5 of the Real Estate Settlement Procedures Act of 1974, into a single, integrated disclosure." The Bureau started this rulemaking process in 2011, issuing a final rule in November 2013 and an implementation date of August 1, 2015, which is now just 107 days away.

This regulation is more than just two new disclosure forms. It represents a paradigm shift in the way real estate settlements occur in this country. Since finalizing this regulation, the title insurance and real estate settlement industry has focused on implementation of these new forms and regulations. I am confident that ALTA's members will be ready for August 1. Our industry and software developers have worked tirelessly since 2013 updating their software and business processes to comply with this regulation. These software programs are wrapping up their beta processes right now and are expected to deliver final software to customers between April and June of this year. All of our training and implementation will take place during what the National Association of Realtors has determined is the busiest time of the year for real estate closings.[2] Unfortunately, our industry's comprehensive preparation efforts may not ensure that real estate transactions will not be disrupted beginning August 1.

Nancy McNealy, the settlement agent from Beltsville, Maryland that I spoke about in my introduction, says that "it is costing a small fortune for most title companies to re-tool to meet the new August requirements." Nancy needed to switch software providers in order to properly support the TILA/RESPA changes. With her new provider, the cost to retrieve old files and continue to access her old database is costing nearly $3,000.00. The cost of the new software and its installation on new computers is about an additional; $5,000.00. For Nancy, that $8,000 in expense for her roughly $156,000 in gross revenue represents a 5% increase in cost of doing

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[1] 15 U.S.C. §1601.

[2] Hale, Danielle. "Part 1: EHS in 2014 by the Numbers – Popular Closing Dates." *Economist Commentaries: National Association of Realtors*, 12 Jan. 2014. http://economistsoutlook.blogs.realtor.org/2015/01/12/part-1-ehs-in-2014-by-the-numbers-popular-closing-dates/ (last accessed 09 Apr. 2015).

business for one regulation in 2015 alone. These software updates ensure that Nancy's company is compliant with the regulation and can send information needed for the real estate transaction to mortgage lenders and other involved parties.

**Need for Formal Hold Harmless Period from August 1 to December 31**

We remain appreciative that the Bureau has provided our industry with 21 months to reform our processes and train our staff to meet these new regulatory demands. However, we know from implementing past regulations that there will be a learning curve and unforeseen issues once the new forms are used in real homebuyer transactions. Therefore, we request that the Bureau publicly commit to making August 1 through December 31 of this year a hold harmless period for enforcement.

I want to thank you, Chairman Neugebauer, and Housing and Insurance subcommittee Chairman Luetkemeyer, on behalf of myself and our ALTA members, for your leadership on this issue and helping us make the case for a hold harmless period to CFPB Director Cordray. I ask the other members of this committee to join Representatives Neugebauer and Luetkemeyer and formally request that the CFPB provide a formal hold harmless period through December 31.

A hold harmless period will allow industry to adapt their business processes comply with this regulation without the fear of potential enforcement actions and class action lawsuits if they struggle in the first few months of using the new forms. In the absence of a hold harmless period, it is likely that some mortgage lenders and settlement service providers will initiate restrictive risk management tactics. This might include limiting access to financing and settlement services in small communities, especially considering many of the unanswered questions that exist regarding compliance with this regulation. For example, it is currently unclear how to properly issue a new closing disclosure if the settlement is delayed due to an unforeseen event like the basement flooding the day before the closing. Without more clarity, the result is likely to leave homebuyers with less flexibility to obtain the deal they bargained for and potentially fewer companies to work with.

To be truly effective, a hold harmless period needs to be accompanied by a commitment from the CFPB to work with industry to gather data about implementation. The Bureau should also provide written guidance to address common industry implementation hurdles that emerge between now and the end of the year. The Bureau's Official Interpretations, compliance guides and webinars on the regulation have been very helpful to industry but they are not comprehensive. Written guidance is needed in many areas to clarify the regulation. We urge the Bureau to commit the resources to providing this written guidance.

**Fix Requirement Inaccurately Disclosing Title Insurance Premiums to Homebuyers**

The new TRID forms prohibit our industry, by law, from disclosing the actual cost of title insurance policies the homebuyer will pay at closing. This is the only cost disclosed at closing that the CFPB prevents consumers from receiving their actual charge.

In the majority of states, when a homebuyer purchases a lender's title insurance policy concurrently with an owner's title insurance policy, the lender's policy is typically issued at a discounted rate (often called "simultaneous issue pricing"). This discount is offered because much of the title search, examination and underwriting that goes into preparing a lender's title insurance policy also supports the owner's policy.

However, in all transactions, TRID requires lenders and/or settlement agents to disclose on the Loan Estimate and Closing Disclosure the lender's title insurance premium at its full rate even though a discount exists that benefits the homebuyer. Conversely, TRID then requires the owner's title insurance premium to be inaccurately disclosed on the forms. As the example

## California

Here is how the rule works when applied to a transaction where the sales price is $200,000 and there is a $190,000 loan:

| The Rule | vs. | Reality |
|---|---|---|
| **OTP on Closing Disclosure = $676.00**<br>(OTP Premium) $902.00<br>(LTP Simultaneous Premium) + $409.00<br>(Full LTP Premium) - $635.00 | | **OTP Actually Charged = $902.00**<br>(OTP Premium) |
| **LTP on Closing Disclosure =$635.00**<br>(Full LTP Premium, with no discounts for Simultaneous Issue) | | **LTP Actually Charged = $409.00**<br>(LTP Simultaneous Premium) |

**Terminology Key:**
**OTP:** Owner's Title Insurance Policy
**LTP:** Lender's Title Insurance Policy

**LTP Simultaneous Premium:** a discounted lender's title insurance premium that is issued in accordance to promulgated state rates or insurance company filed rates when both a lender's and owner's title insurance policies are simultaneously issued

shows below, the result is that in most states, the Closing Disclosure will not provide consumers with accurate disclosures of their title insurance costs.

The Bureau could easily resolve this issue by requiring mortgage lenders and settlement agents to disclose the actual title insurance premium rates required in the state in which the real

property is located. We are not proposing to change the regulation's requirements surrounding the disclosure of title premiums on the Loan Estimate, which would require an amendment to the regulation. Rather, the Bureau can modify a section of the Official Interpretation:

**Comment 38(g)(4)-2:**

> In a jurisdiction where simultaneous issuance title insurance rates are permitted, any owner's title insurance premium disclosed under **§ 1026.37(g)(4) or** § 1026.38(g)(4) is calculated by using the full owner's title insurance premium~~, adding any simultaneous issuance premium for issuance of lender's coverage,~~ and then deducting ~~the full premium for lender's coverage disclosed under § 1026.38(f)(2) or (f)(3)~~ **any policy cost differences due to the simultaneous purchase of a lender's title insurance policy**.

We appreciate that the Bureau is attempting to show consumers the marginal cost of purchasing on owner's title insurance policy; however, we are greatly concerned about the confusion it will cause consumers. In absence of a solution, the Bureau is causing our industry to inaccurately disclose consumers' costs for title insurance and exposes ALTA members to potential class action lawsuits and market conduct examination errors—not to mention actively dissuade homebuyers from purchasing financial protection for their largest investment.

Accurately disclosing the price of title insurance policy premiums will also help the title industry comply with state regulations. Under state insurance laws, title insurance companies are only allowed to charge the policy premium rates promulgated or filed with the state. If the Bureau declines to fix this problem, our industry is likely to address this legal requirement to knowingly disclose incorrect title insurance premiums by providing a second disclosure to the homebuyer showing the actual premium cost. Our industry will need this additional disclosure to prove to state insurance regulators and potential class action plaintiffs that they were charged the correct policy rates under state insurance law. These additional disclosure forms will likely contribute to homebuyer confusion about the actual costs of their title insurance policies, closing costs and homeownership in general.

We urge the Bureau to address this issue immediately. ALTA believes that the best way to reduce homebuyer confusion regarding the disclosure of title fees under the Rule is to modify the Official Interpretations to allow industry to disclose the actual title insurance premiums on the Closing Disclosure.

**Improve the way the Bureau protects consumers and works with businesses**

While ALTA members are not directly supervised by the Bureau, we are indirectly regulated through the Bureau's oversight of both depository and non-depository mortgage lenders. Our industry is most acutely feeling the impact of CFPB Bulletin 2012-03 on service providers.[3] This bulletin restated longstanding guidance from other federal regulators about the expectation that lenders should oversee their business relationships with service providers in a manner that ensures compliance with federal consumer financial law.

[3] http://files.consumerfinance.gov/f/201204_cfpb_bulletin_service-providers.pdf

While other federal regulators have promulgated voluminous guidance to both depository and non-depository mortgage lenders on how to manage the risks affiliated with third-party service providers, the CFPB's bulletin only provided lenders with two and a half pages of guidance. This lack of guidance from the Bureau, compared to the sixteen pages of guidance in from the Office of the Comptroller of the Currency (OCC) and fourteen pages of guidance from the Federal Reserve Board in 2013, has left lenders unsure of what kind of risk management the CFPB would require of lenders and how the CFPB would enforce its expectations. Lenders are left without a clear path, and many are still feeling their way through the risk management process.

This lack of guidance has consequences for our homebuyers. Recently, a Wisconsin title company talked to ALTA about their customers, Kenneth and Danielle, who were scheduled to buy a $260,000 home in the Village of Caledonia, Wisconsin, on March 15. Two days before the scheduled closing, the title company's closing officer received an email from a loan processor at the mortgage company. The email directed the closing officer to the website of an unknown company requesting more information before the title company could continue conducting real estate settlements for this particular mortgage lender. The website asked the closing officer to provide personal information including her Social Security Number, authorization for a credit check, name of her personal banking institution, her personal bank account number and an authorization for her bank to speak with them. A letter accompanied this request from the mortgage lender that read:

"[Our company] has been hired to conduct vendor management services on behalf of the mortgage lender for whom you are handling funds and documents. All mortgage lenders and banks are required by regulation to conduct comprehensive checks and ongoing risk monitoring of settlement agents for consumer protection and data privacy and security purposes. We thank you for assisting lenders in meeting their legal requirements to protect consumers."

When the title company contacted the mortgage lender to say that the information requested was well beyond what would be required by title insurance and settlement industry best practices, our ALTA member reported, "the mortgage lender stated that use of this vetting company was required, and our title company declined to go forward. We assume that the mortgage lender then placed their title and closing order with a different company and we know that the homebuyer's closing was delayed for several days."

Kenneth and Danielle's closing was scheduled to occur on March 15th but was delayed until 5pm on March 19. This delay didn't protect Kenneth and Danielle from financial harm. The delay was simply because a mortgage lender hired a third-party vendor, who is unregulated to request the Social Security Number, and personal bank account information, of another third-party vendor [the title company], who is regulated and licensed by states department of insurance. The unregulated vendor wanted authorization to check a regulated and licensed vendor's personal credit, the name and account number of her personal banking institution, and an authorization for her bank to speak with them. This is not commonsense consumer protection – this is overregulation.

A second example is from October of 2014 when a Missouri title company received a title order from a homebuyer, John, who was refinancing his home in Chesterfield, Missouri. In

order to proceed, the mortgage lender required the staff of the state-regulated and state-licensed vendor, the title company, to provide the same non-public personal information to another vendor who is not regulated, in order to process the title order. It wasn't until the Missouri title company said that they, "would resign from the transaction and contact the borrower to let them know why before [the mortgage lender] agreed to remove the requirement and allow the title company to handle the transaction."

These two examples of consumers being affected by overregulation was not the fault of either mortgage lender. These examples show that many lenders are still operating blindly with regard to their risk management process because of a lack of guidance from the CFPB.

In the absence of this guidance, and to assist our business partners' understanding of our industry, ALTA took the lead and developed a tool in 2012 to help the industry illustrate to homebuyers and lenders the industry's professionalism and best practice standard to help ensure a positive and compliant real estate settlement experience.

Today, ALTA's Title Insurance & Settlement Company Best Practices are becoming an industry standard of prudent business practices that lenders and settlement agents are adopting as the backbone of their service provider oversight program. These Best Practices are designed to meet market demands while being flexible enough to be adopted by all companies in the title and settlement industry, regardless of business size.

The Best Practices includes the following seven pillars:

1. Establish and maintain current license(s) as required to conduct the business of title insurance and settlement services
2. Adopt and maintain appropriate written procedures and controls for Escrow Trust Accounts allowing for electronic verification of reconciliation
3. Adopt and maintain a written privacy and information security program to protect Non-public Personal Information as required by local, state and federal law
4. Adopt standard real estate settlement procedures and policies that help ensure compliance with Federal and State Consumer Financial Laws as applicable to the settlement process
5. Adopt and maintain written procedures related to title policy production, delivery, reporting and premium remittance
6. Maintain appropriate professional liability insurance and fidelity coverage
7. Adopt and maintain written procedures for resolving consumer complaints

ALTA's Best Practices have gained the support of both large mortgage lenders (like Wells Fargo and SunTrust Bank) as well as community lenders (such as BancorpSouth Bank and FirstMerit Bank).

**Regulatory Reform Proposals that Improve How the Bureau Interacts with and Regulates the Title Industry**

While ALTA's Best Practices provide much needed guidance to the market, more should be done by the Bureau to fill this void. This is why ALTA supports three bipartisan legislative proposals to improve not only the way the CFPB receives feedback from industry about its regulatory proposals, but also the way the CFPB provides industry with much needed guidance about its expectations regarding compliance with federal consumer financial protection law.

First, Congress should pass H.R. 1195 as soon as possible. This bipartisan legislation introduced by Rep. Robert Pittenger and Rep. Denny Heck would establish a small business advisory board at CFPB, similar to those established for outreach to community banks and credit unions. This advisory board would give small businesses, like Nancy McNealy's in Beltsville, Maryland, a seat at the table when the Bureau is considering additional regulations that may negatively affect her business and consumers. Advisory boards provide clear, formal and open channels of communication between Bureau staff and industry. Since the Bureau only supervises depository institutions with more than $10 billion in assets, the CFPB created an advisory board for community banks and credit unions to promote regular contact with these institutions. Creating a similar advisory organization for nonbanks will allow these smaller institutions to report, advise or consult with the Bureau on a regular basis.

ALTA members applaud the House Financial Services Committee for approving H.R. 1195 on March 26 by a bipartisan vote of 53–5. We will continue to urge members of Congress from both sides of the aisle to support this commonsense legislation as it moves to the floor of the U.S. House of Representatives.

Second, Congress should approve legislation that directs the CFPB to establish procedures for issuing advisory opinions to the financial service providers it regulates. The best ways to protect consumers and produce good outcomes for their financial decisions are to discourage bad acts through enforcement while at the same time to also encourage good behavior. Today, the Bureau takes its enforcement role seriously, but we encourage it to take their ability to promote good practices seriously too. An advisory opinion provides certainty to those complying with federal consumer financial law in real-life situations.

Close to 20 other federal agencies issue advisory opinions. This type of guidance, issued in response to a specific request, would improve certainty about whether a proposed design, operation or maintenance of consumer financial product would be prohibited under federal consumer law.

These advisory opinions should be made available to the public through the CFPB website. However, before publication of any advisory opinion, the CFPB should redact specific information about the requesting individuals or entities, and about any individuals or entities associated with the requestor, to the extent that is reasonable to prevent release of any confidential business information or trade secrets.

ALTA members support bipartisan advisory opinion legislative efforts that include specific timeline triggers for the CFPB to respond officially to an advisory opinion request. In addition, we support a fee structure that could be levied on the advisory opinion requestor in order to offset the additional staff the CFPB would need to complete accurate advisory opinions.

Finally, Congress should consider actions to improve CFPB transparency in the processes used to create bulletins, guidance documents and enforcement actions. In all three instances, the CFPB does not encourage public feedback to these performed actions. Substantive or legislative rules issued by federal agencies, like the CFPB, must undergo a public notice and comment rulemaking under the Administrative Procedures Act (APA). Comments are published in a public forum to promote transparency of rulemakings. Regulations issued by the CFPB benefit from public input and feedback. Receiving public input also makes regulations more effective, resulting in fewer unintended consequences on small businesses and consumers.

Whether a comment is provided to the CFPB through a bulletin, a guidance document or an enforcement action, this feedback should be made available to the public. In many cases, soliciting transparent public comments on an issue promotes discussion that leads to better long-term policy outcomes. Members of Congress employ these tactics when they handle constituent calls and letters each day.

As you continue to consider various regulatory reforms in the coming months, please remember the stories I have shared today from Maryland, Missouri and Wisconsin. Unfortunately, these complications are replicated in real estate transactions throughout the country as our members work to comply with new state and federal laws. Thank you for inviting me to testify today. ALTA is eager to serve as a resource to this Subcommittee, and I am happy to answer any questions.

United States House of Representatives

Committee on Financial Services

Subcommittee on Financial Institutions
and Consumer Credit

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Hearing entitled:

"Examining Regulatory Burdens on
Non-Depository Financial Institutions"

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Wednesday, April 15, 2015

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Statement of Justin G. Friedman

American Financial Services Association

Chairman Neugebauer, Ranking Member Clay and Members of the Subcommittee:

Good Afternoon. My name is Justin Friedman and I direct government affairs for the American Financial Services Association or AFSA, the nation's oldest consumer credit association which is celebrating its 99th anniversary in 2015. I am pleased to be here today to provide testimony to the Subcommittee as it examines regulatory relief for non-depository financial institutions and to discuss proposals to improve the structure of the Consumer Financial Protection Bureau ("CFPB" or "Bureau"). We wish to thank Chairman Neugebauer and Ranking Member Clay for holding a hearing on this issue, which is of keen importance to the consumer credit industry and the households we serve.

**Statement of Interest**

Founded in 1916, AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. The association encourages and maintains ethical business practices and supports financial education for consumers of all ages. AFSA has provided services to its members for nearly a century. Our 390 member companies include consumer and commercial finance companies, motor vehicle finance companies including the captives of the automakers, card issuers, mortgage lenders, industrial banks, and other financial services companies that make credit available to consumers and small businesses.

AFSA member companies offer a broad array of financial products, including personal installment loans, retail and commercial sales finance, credit and payment cards, residential mortgages, vehicle loans and leases, and floorplan finance for dealers. Our members provide approximately 80 percent of the nation's vehicle financing. In general, finance companies are responsible for one of every five dollars of consumer credit.[1]

**Consumer Finance Companies Serve a Broad and Important Market**

While depository institutions play a vital role in the economy and the consumer credit market, Federal Reserve Board statistics show that a substantial share of non-mortgage consumer credit is provided by finance companies and others who raise funds through securitization. In fact, for non-revolving lines of credit, finance companies and banks hold roughly equal shares of the overall pie – about one quarter each. Both are smaller than the share held by the federal government, which of course dominates the student loan market.

Finance companies have a long history of meeting the credit needs of consumers – from buying a car to get to work, to paying college costs for a son or daughter. Finance companies are licensed by each and every state where they do business, so the CFPB has added a complex new layer of federal oversight to our members' existing regulatory regime.

The principal types of credit offered by consumer finance companies are motor vehicle finance and traditional installment loans.

[1] Federal Reserve Board, G.19 Report on Consumer Credit Outstanding (February 2015)

While much has been written and said about the abuses found in certain forms of short-term, small-dollar lending, policymakers should recognize that traditional installment loans are a time-tested and beneficial form of credit for working Americans. I am talking about fixed-rate, fully-amortizing personal loans, which are repaid in equal monthly installments of principal and interest. Traditional installment loans are the safest, most responsible form of small-dollar lending and have been for many decades.

The average loan is for $1500, the average monthly payment is $120, and the average term is 15 months. These are "plain vanilla" loans with transparent, easy-to-understand terms, due dates and payment amounts. Installment lenders report payment behavior to credit bureaus, which helps consumers to build or repair their credit history.

Borrowers commonly use these loans for vehicle repairs, to purchase household appliances and cover unexpected medical expenses -- the everyday items and services essential to living a productive and enjoyable life.

AFSA members make automobile financing available directly through branch-based lending and indirectly through dealerships. Their provision of credit helps keep the automotive market a strong, competitive and integral part of the American economy.

While our industry is focused on providing a positive experience for the consumer, it also provides a reliable source of liquidity for auto dealers. Specialized auto lenders do not withdraw from the market during economic downturns, unlike banks that have safety and soundness concerns which may compel them to curb auto lending during times of turbulence.

**The Role of State Regulators in Overseeing Non-Depositories**

The trope that non-depository lenders are "unregulated" is simply untrue. Like the insurance industry, non-depository institutions were simply regulated by someone else. The states have regulated installment lenders since 1880 – 33 years before the passage of the Federal Reserve Act, 53 years before the passage of the Federal Deposit Insurance Act, and 130 years before the creation of the CFPB.

The framework of modern consumer lending stems from the passage of the Uniform Small Loan Law, first enacted in California in 1909, and eventually throughout the country. The Uniform Law Commission first promulgated the Uniform Consumer Credit Code in 1968 to provide for comprehensive regulation of consumer credit by the states.

The National Association of Consumer Credit Administrators (NACCA) was formed in 1935 to build the capacity of state regulators of consumer credit and to facilitate the administration of laws governing these agencies. It continues to do so today.

The creation of the CFPB imposes new, often duplicative, federal regulatory burdens on these state-regulated entities.

State regulators have a familiarity with local and regional circumstances and issues faced by lenders. This knowledge, along with their geographic proximity to a given lender and the markets in which it operates, means that a state regulator is often the first to identify emerging issues, practices or products that may need further investigation or may pose additional risk to the financial industry and its customers.

Currently, the CFPB may promulgate regulations impacting state-licensed companies without:

- Finding that existing state law or regulation is inadequate;
- Determining an estimate of the number of state-licensed or supervised entities to which the regulation will apply;
- Describing the projected reporting, recordkeeping and other compliance requirements; or
- Identifying the relevant state statutes, regulations and enforcement proceedings with which the new federal regulation may duplicate, overlap or conflict.

No one size fits all. Credit needs, average income and demographics vary from state to state. A given state legislature may choose to allow a product or tolerate a pricing regime of which another state does not approve. Where it comes to state-licensed consumer finance companies, we believe that decision is best left to each state capital to decide what is beneficial to their constituents.

Thomas Jefferson put it best: "Our country is too large to have all its affairs directed by a single government. Public servants at such a distance, and from under the eye of their constituents, must, from the circumstance of distance, be unable to administer and overlook all the details necessary for the good government of the citizens; and the same circumstance, by rendering detection impossible to their constituents, will invite public agents to corruption, plunder and waste."[2]

**Supervisory Privilege**

On behalf of AFSA's member companies, I wish to thank the Committee for its help in enacting H.R. 5062, the Examination and Supervisory Privilege Parity Act of 2014, legislation that clarified the sharing of information between federal and state agencies that license, supervise or examine nonbanks offering consumer financial products or services.

This legislation resolved a regulatory disparity between depository and non-depository institutions, recognizing the unique situation of non-depositories and their relationships with state regulators. We are pleased that the legislation was introduced and passed in a bipartisan manner.

AFSA hopes that this effort can serve as a model for future proposals to reform the CFPB.

[2] Thomas Jefferson to Gideon Granger, 1800. The Writings of Thomas Jefferson, (Memorial Edition) Lipscomb and Bergh, editors. 10:167

**A Review of the CFPB's Governance**

AFSA believes that the CFPB's current governance structure is flawed and it should be replaced by a bipartisan, multi-member commission – as is the norm for virtually all independent regulatory agencies of the federal government.

The CFPB's mandate is to regulate the offering and provision of consumer financial products or services and enforce the Federal consumer financial laws.

Unlike most independent regulators, the Bureau is not governed by a bipartisan board. This has been the model for more than a half century for federal agencies that have consumer protection responsibilities (*e.g.* the Federal Reserve Board, Federal Deposit Insurance Corporation, Federal Trade Commission, Consumer Product Safety Commission, Securities and Exchange Commission, and the Commodity Futures Trading Commission). The CFPB is headed by a single political appointee.

Although nominally housed within the Federal Reserve, the Federal Reserve Board of Governors cannot direct activities, terminate staff or review regulatory or enforcement activities. Unlike the traditional independent agency model, the CFPB is guaranteed a percentage of the Federal Reserve Board's budget, depriving Congress of fiscal oversight through the annual appropriations process.

Once a Director of the CFPB is confirmed by the Senate, even the President of the United States has no effective control over the position other than termination for cause.[3] In contrast, the norm among independent agencies structured as commissions is that a new President may designate his or her choice of a chairman.

**The Structure of the CFPB should be Reformed**

AFSA congratulates the Financial Services Committee on passing 11 bipartisan regulatory relief bills in March. We believe that H.R. 1195, the Bureau of Consumer Financial Protection Advisory Boards Act, will help small business. AFSA also welcomes Chairman Neugebauer's introduction of H.R. 1266, the Financial Product Safety Commission Act of 2015, which alters the CFPB structure to a bipartisan, five-member commission appointed by the President.

Twice before, the House has wrestled with the CFPB single director structure. In the 112th Congress, H.R. 1121, the Responsible Consumer Financial Protection Regulations Act of 2011, was reported by the Committee. In the 113th Congress, the House passed H.R. 2446, the Responsible Consumer Financial Protection Regulations Act of 2013, which would have amended the Dodd-Frank Act to replace the CFPB Director with a five-person commission – one of whom would be the Federal Reserve's Vice Chairman for Supervision, lending necessary experience in bank regulation, plus four other members who "have strong competencies and experiences related to consumer financial protection."

[3] The Dodd-Frank Act even provides that congressional testimony by the Bureau's Director must provide a regulatory Miranda Warning that it does not necessarily represent the views of the President, and the President is prohibited from reviewing any legislative recommendations or comments the CFPB may submit.

While we believe this was a step forward, the previous bills did not address state-licensed entities and the substantial portion of the consumer credit market they serve. As noted above, state regulators are closest to these markets and possess important insight into the practices or products of the lenders they license. State regulators are best positioned to investigate issues that may pose risks to local consumers.

AFSA recommends that at least one member of any CFPB board should have state bank or consumer credit supervisory experience. A similar approach has worked effectively at the Federal Deposit Insurance Corporation and would be appropriate for the CFPB. We believe the unique qualities of credit unions and state-chartered banks require similar representation.

Thus, the new commission could be composed of the Federal Reserve's Vice Chairman for Supervision; a member with non-depository consumer credit supervisory experience; a member with state bank supervisory experience; a member with credit union supervisory experience and a public member possessing strong competencies related to consumer financial protection.

Some fear that any structural reform would harm the mission of the CFPB, but AFSA believes the converse to be true. An agency directed by a commission with a bipartisan membership is better insulated from electoral politics, and most likely to produce sustainable public policy that will protect consumers while promoting access to credit.

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AFSA and its member companies welcome the opportunity to work with Congress as it addresses these important issues.

**Appendix: AFSA Members' Customers Value their Services**

It is easy for policymakers to become detached from the lives of individual consumers, and to forget that legislative and regulatory initiatives have intended and unintended consequences impacting the people they are intended to protect. For this reason, AFSA believes the following narratives from our customers merit sharing:

> *[AFSA member company] offered me a loan after I had been turned down by other companies and banks. They worked with me to allow me to extend my loan during a period when I was having difficulty paying my bills. We need more companies that are willing to take risks on people with less than perfect credit scores. For them, I am personally grateful.* — Joyce from Marion, Iowa

> *[I was] coming from a small town of Mississippi, for a new beginning [and I was] in need of a dependable ride. With little money on hand, [a] number of places turn me down for a loan, and the Repos I looked at was [sic] just not worth driving off the lot. Two weeks pass by [and then] on TV I saw [AFSA member company]. The very next day, by the end of the day, I was happy riding [sic]and [had] cash in my purse. Thank you [AFSA member company for blessing me.* — JoAnn from Mississippi

> *As my medical bills and other bills were piling up, I just couldn't keep up. The installment loan that I qualified for at [AFSA member company] ...helped me get back on my feet. Thank you to [the company]!* — Tim from Cedar Rapids, Iowa

> *Being a single mom can be a challenge. I've worked hard for six years to provide my daughter [with] the very best, but with just a single income, no child support, and no family, things can get tough. When I approached the bank for a loan, I was turned away and referred to [AFSA member]. They have helped me in so many ways.* — Te from Marion, Iowa

> *Several years ago, we purchased a new home on contract in a great neighborhood and school district. My wife and I both had secure jobs of 15 years, but we had been through some challenging times and had to file [for] bankruptcy. In the contract we had one year to secure our own financing. Everywhere we went we were told we had to be out of bankruptcy for two years before we would be eligible for a new mortgage loan. When the first year ended, the contract owner called the contract due. We were so afraid that we would lose our home. Then we found [AFSA member company]. They took our application, analyzed our circumstances and said they could help. [AFSA member company] financed the balance of our contract and told us that when our bankruptcy was at least two years old we could look at refinancing the loan with no penalty. We were able to save our home and pay off the contract owner.* — Customer from Long Grove, Iowa

> *"We have had numerous loans with [AFSA member company] over several years. Our experience with [AFSA member company] has been both pleasant and rewarding. The personnel there has always been courteous and efficient. We chose a traditional*

*installment loan because it suited our needs as far as being quick to close with no long waiting period for approval and time-consuming paperwork prior to the closing. The traditional installment loans have helped us reach our financial goals in business and our personal finances. We could not have received the financing we needed as quickly as we needed it with any other loan process.* — Ronnie from Purvis, Mississippi

PRESERVING FAIR STANDARDS FOR COMMUNITY LENDERS

TESTIMONY

PAULINA SEPULVEDA MCGRATH

THE COMMUNITY MORTGAGE LENDERS OF AMERICA

HOUSE SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

HOUSE COMMITTEE ON FINANCIAL SERVICES

APRIL 15, 2015

I am Paulina Sepulveda McGrath, President of Republic State Mortgage Co. in Houston. I am here today as the Chairperson of the Community Mortgage Lenders of America, a trade group representing both small mortgage bankers and community banks with mortgage lending expertise. CMLA is pleased Congress is moving forward with regulatory streamlining for community banks, and we support those measures.

However, if Congress does not provide the same streamlining for community-based, non-depository mortgage lenders this effort will fail consumers and small businesses in every community in our country.

These lenders originated approximately 40 percent of all conventional loans and roughly 50 percent of all loans insured by the Federal Housing Administration and Department of Veterans Affairs in 2014. We are a key piece of the mortgage market, especially for consumers looking to get on the first rung of the economic ladder and for those borrowers looking for, or needing, more personalized service.

Unfortunately, the current regulatory burden is driving consolidation among small mortgage lenders. If this consolidation continues, the reduced competition will lead to even higher costs and consumers will have fewer choices. As a country, we need to find a way to serve – with careful and safe underwriting – more families in their homeownership needs, particularly first-time homebuyers. If we cannot, these

families will continue to pay ever-increasing rents that are outstripping income gains.

Remember: Dodd-Frank's goal was certainly to make lending safer for consumers; however, as we were told in 2009, the law was intended to regulate most closely the largest lenders and the bad actors. Subsequent experience with this statute shows it lacks the flexibility to distinguish the level of regulation necessary for lenders of different sizes, business models and performance records. Consequently, it levies the regulatory burden on everyone, including small lenders that operate in a prudent manner and who simply cannot amortize large fixed costs onto a relatively modest volume of mortgage lending.

We think it is important for Congress to take reasonable steps to help preserve small lenders as an important segment of the mortgage lending industry. Without these steps being taken, we are extremely concerned that the consolidation we see today will strengthen and consumers will face fewer choices among lenders, higher costs and the sort of impersonal, bureaucratic service so prevalent among larger lending organizations. We do not believe such an outcome would in any way be an advancement of consumer protection.

The CMLA would like to introduce a concept that will spur more community lending while not diminishing consumer protections: why not provide some targeted relief for small lenders, which have no recent enforcement actions, and which originate primarily loans that meet the Qualified Mortgage (QM) standard contained in the Truth-in-Lending statute? Why not streamline certain regulations for these lenders, which recognizes their unique role in the lending market and benefits the borrowers whose home financing needs they serve?

We propose that lenders would receive specified relief, so long as they remained (1) small, with (2) most of their annual loan origination volume composed of QM loans, and (3) only as long as they continue their excellent lending records. (If a lender grew too large, decided to pursue a non-QM market, or received an enforcement action, it would lose the streamlined regulation.)

If Congress adopted a framework like this, it would spur more community lending while maintaining the consumer focus intended by policymakers. The consolidation and shuttering of community mortgage lenders would subside, providing consumers more choices, better pricing and better service. This is most crucial for our country's underserved areas and communities – from the rural areas to the inner city.

What sort of streamlined regulations would make sense? The CMLA is proposing a series of regulatory changes to preserve strong consumer protections while, at the same time, providing prudent and safe regulatory relief for small and mid-sized lenders.

The first is a very straightforward, common sense type of change. Current disclosure rules require new disclosures if there is a change – for good or bad -- in fees, costs or interest rate cause the Annual Percentage Rate (APR) of a loan to change by more

than a minimal amount prior to the close of the loan. A new disclosure must be made to the borrower and a three-day period must elapse prior to the closing of the loan following the revised disclosure. This is an appropriate consumer safeguard when the change results in a higher APR and therefore higher costs. However, it makes no sense when the change is resulting in a lower APR and therefore lower costs to the borrower. We recommend Congress mandate that the three-day waiting period be waived when a change results in a lower APR for the borrower than previously disclosed by the lender.

Vendor oversight requirements are another good example of the excessive regulatory burden faced by midsize and smaller mortgage lenders. Current rules do not differentiate between large and small lenders; instead, the rules levy the same vendor oversight duties and responsibilities on small to midsize mortgage lenders as they do on large banks.

Because the costs of conducting ongoing oversight and review of vendors are far more onerous for, smaller lenders they tend to choose large, national vendors. This decision provides smaller lenders with greater assurance of the vendor's integrity. Nevertheless, they must vet each of these national vendors on a regular basis, duplicating oversight that takes hundreds of staff-hours per year for each lender. Moreover, the impact of these necessary business decisions means that smaller, local vendors that traditionally provided these services are being shut out and job losses in these communities are meaningful.

Third, CFPB examinations are an important enforcement tool for the Bureau with large lenders and those lenders that may have broken the rules. However, the Dodd-Frank statute does not provide clarity or prioritization for the CFPB in the marketplace.

We suggest Congress establish a statutory priority for CFPB examinations, directing the Bureau to conduct examinations of small lenders only if there has been a referral by another regulator. Small lenders are routinely examined by a number of different regulators. Small banks are examined by state banking regulators and the FDIC at a minimum. Small non-depository lenders are examined by the regulator of each state in which they operate. In addition, many small non- depository lenders are approved FHA and VA lenders, as well as by Fannie Mae and Freddie Mac, and are examined by each of these organizations. Why not say that the disproportionate CFPB exam prep costs, including mock audits, together with the costs of the actual examination will not fall on small lenders unless a referral came from one of the existing regulators and agencies overseeing these lenders. Remember: the CFPB will still be able to go where it is most needed; the provision will help it focus its resources where these resources will truly add to consumer protection.

Fourth, the current rules around servicing provide no relief for nonbank servicers doing a good job. Nonbank lenders typically contract with a subservicer for the servicing of their loans in order to keep costs reasonable and offer a high level of service to borrowers. CMLA would propose that Congress statutorily define the definition of small servicer. We would further propose that relief granted to small

servicers meeting this statutory definition not differentiate between small servicers that perform all servicing functions internally, and those small servicers that utilize contract subservices to keep costs low and consumer service high. Again, this streamlining would be for lenders of small size, doing QM lending, with good track records. We should not penalize these lenders solely because they use subservicers.

*On these policy recommendations above, CMLA is working closely with the Community Home Lenders Association, an association exclusively representing nonbank mortgage lenders.*

Fifth, CMLA suggest an amendment to the SAFE Act regarding the licensing of loan originators. Currently loan originators employed by non-depository lenders are licensed by state regulators. Those originators must take educational courses, pass an examination conducted by the state regulator and undergo a background check. Loan originators employed by depository lenders are registered in a database maintained by Federal banking regulators. Other employment requirements are left to the discretion of the depository employer, who will usually conduct a similar background check and utilize internal or external training courses to ensure the appropriate industry knowledge among their loan originators.

In every local community across the U.S., consumers interact on a daily basis with registered and state-licensed loan originators. These originators – regardless of which Federal or State regulatory body has oversight of their employers – perform the same tasks, working with consumers to assess their home finance needs and then taking the steps necessary to qualify the consumer for the financing that will allow them to purchase the home of their choice.

As you can appreciate, in the employment marketplace, it is a difficult process for a non-depository lender to recruit and employ a loan originator from a depository lender despite the fact of nearly identical duties and consumer interaction. Once a loan originator employed by a depository lender leaves that job and takes an identical position with a non-depository lender, usually within the same geographical market, they cannot originate any loans until they take the courses, and pass the examination and background check required by state regulations. By contrast, a licensed loan originator employed by a non-depository or a depository, can resign their position on a Friday and begin working for a depository as a registered loan originator the following Monday.

CMLA proposes that Congress amend the SAFE Act to direct state regulators to issue a 180-day transitional license to a loan originator registered with an insured depository who is hired by a non-depository lender. This transitional license would allow the loan originator to continue their employment for the period of time it takes them to satisfy the state licensing requirements.

Effect of Increasing Compliance Costs

We recently conducted a survey among our members to determine the impact of increasing compliance costs. We found that compliance costs on average had

increased nearly 200 percent for small lenders since 2010 on an aggregate basis and approximately 125 percent on a per loan basis. Unfortunately, some of these costs have been passed onto consumers. Lenders have also absorbed a portion of these costs. However, to the extent the increases in these costs have made it impossible for small lenders to continue to operate economically, these smaller lenders have been forced to sell or shut down their companies, thereby continuing the reduction in consumer choices.

Obviously, a very large bank can more easily absorb compliance costs. Moreover, it is just as obvious that there is greater need and justification for stronger regulation of a large bank's mortgage lending. As we saw before and during the financial crisis, large institutional lenders can drive market behavior, and their failures can have devastating financial consequences for the market. Therefore, a tighter regulatory check on their activities is amply justified.

By contrast, most small mortgage banking companies are independently owned, do not retain a loan portfolio and have no access to bank deposits to fund operations and no access to the Federal Reserve window for liquidity. Instead, our lending operations are financed by warehouse lines of credit, which cost four to eight times more than insured deposits and overwhelmingly require personal guarantees by the company owners. In effect, our lenders risk their own capital in making mortgages and thus, our lending practices and quality control constitutethe primary safety net should a loan fail.

Ask yourself: how did these community lenders survive the worst downturn since the Great Depression? Although some community banks received TARP money, not one of the mortgage bankers did--yet they are still here today. How could this be? The answer is we continually and routinely executed with higher underwriting standards--and did not take advantage of our borrowers with shoddy products that provided short-term payoffs and long-term pain.

The last few years have been a struggle to continue to serve our borrowers. We are hiring more compliance and non-consumer facing personnel than ever before. Given our higher cost of funding, mortgage banking companies are more vulnerable, not less, to the higher fixed costs of legal and compliance operations mandated by Dodd-Frank. The average independent mortgage banker with up to 250 employees has increased compliance staff from two to seven according to our survey, with average annual compliance costs increasing from approximately $432,000 to $1. 3 million. The problem becomes painfully evident. The cost of auditing vendors runs about $75,000 annually. The cost of preparing for a mock audit for a CFPB exam that may or may not ever come is $50,000. Since 2010, CMLA data show that compliance costs per loan have more than doubled--and this, again, is for lenders doing predominantly QM lending, which has its own built-in consumer protections.

When you consider these high fixed costs, combined with other tightening factors such as GSE buybacks, the economics of originating small-balance loans look especially challenging. The Houston Association of Realtors data on home sales in

December 2014 compared to December 2013 show one way the market has been reacting:

- Sales volumes for homes below **$79,999 declined** 19.8 percent, year over year
- Sales volumes for homes $80,000 - **$149,999 declined** 8.1 percent, year over year
- Sales volumes for homes $150,000 - **$249,999 increased** 19.4 percent year over year

  Sales volumes for homes ·$250,000 - **$499,999 increased** 26.1 percent year over year

- Sales volumes for homes $500,000 - **$1 million+ increased** 20.4 percent, year over year

National data tell a similar story; according to NAR data, recent sales of homes in the $250,000 – 500,000 range increased 10 percent from a year ago, while homes valued at $100,000 and below declined by 10 percent, according to the NAR. Our CMLA data show a similar pattern. Some of this divergence is due to jobs and debt pressures at the lower end of the income scale, but some of the lending reflects the fixed costs for any loan and the losses that lenders may take on smaller loans. The inescapable economic fact is that lenders can recover their fixed costs in three ways – through higher fees charged to borrowers, higher interest rates or emphasizing the origination of higher balance mortgages. The first two options make it hard for consumers to buy the home of their choice because of greater out-of-pocket cash demands at closing or a higher monthly payment for the life of the loan. The third option disadvantages moderate-income borrowers and first time buyers who are typically buying smaller, lower cost homes. None of those results appears to advance the cause of consumer protection.

Some people argue that there is good reason to overlook mortgage bankers' need for regulatory relief. They say that since mortgage bankers sell all the loans they originate, and therefore have little or nothing at risk if the loans they originate perform poorly, they do not merit the same consideration.

This is patently false.

There has been a steady stream of repurchase demands issued in the aftermath of the financial crisis. Even if the repurchase demand is without merit, the costs to defend frequently outweigh the loss from the loan. This risk is quite personal to mortgage bankers, taking into account the personal guarantees and the fact that our own net worth is usually tied up in our companies. We have very, very little margin of error, and no access to federally insured funds. Our lenders did not build the business plan of their companies around the origination of Liar Loans, Exploding ARMs, NINJA loans and other toxic products then, and we certainly do not do those types of loans now. Our own money is on the line--which means our

interests are aligned with that of our borrowers: carefully underwritten loans that will perform well over time.

In sum, we commend this Subcommittee and the full Committee for the work to ensure community banks thrive on behalf of local consumers, who depend on us for maximum choices and to keep costs low. We urge Congress to extend meaningful regulatory relief to all small community lenders, and to find ways to empower more lending while not compromising consumer protections. Let us return to the original framework of Dodd-Frank and make regulation work for everyone.

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**Testimony of W. Dennis Shaul**
**Chief Executive Officer**

**On Behalf of the Community Financial Services Association of America**

**Before the**
**United States House of Representatives**
**Financial Institutions and Consumer Credit Subcommittee**
**Financial Services Committee**
**"Examining Regulatory Burdens on Non-Depository Financial Institutions"**

**April 15, 2015**

## I. Introduction

Chairman Neugebauer, Ranking Member Clay, and members of the Subcommittee thank you for inviting me to testify today. My name is Dennis Shaul, and I am Chief Executive Officer of The Community Financial Services Association of America (CFSA). I am here today to testify on behalf of our members, their thousands of employees, and the millions of customers who use our products.

CFSA was formed in 1999 to promote laws and regulations that protect consumers while preserving access to credit options and to support and encourage responsible practices within the payday loan industry. CFSA's member companies represent more than half of all traditional payday loan storefronts across the country, in more than 30 states. Our members provide payday loans to more than 19 million households, as well as a wide range of other financial products and services, including bill payment, check cashing, installment loans, prepaid debit cards, and tax preparation services.

Our members' storefront locations put us in the heart of many financially underserved and underbanked communities including rural and less populated areas, where credit options are not always readily available. CFSA members are heavily regulated. For nearly 20 years, individual states have worked with the industry to enact laws, and also to regulate the product through state supervision, licensing, and audit requirements. Requirements for a state license typically include a bond, background investigations and fingerprinting of company officials, evidence of industry experience, and minimum capitalization and liquidity requirements. State examinations monitor compliance with laws and regulations, and often include a review of loan agreements, customer files, federal and state disclosures, and collection procedures.

In addition, payday lenders are regulated at the federal level under supervision and rulemaking authority of the Consumer Financial Protection Bureau (CFPB or Bureau), and are subject to extensive examinations. Our members actively participate in the CFPB complaint resolution process and regularly invite CFPB employees to their stores to better learn about their products. Additionally, CFSA members are subject to enforcement of federal consumer financial laws by the Federal Trade Commission (FTC).

To serve our customers responsibly, CFSA has developed a set of 13 Best Practices that expect compliance with all applicable state and federal laws. Our members hold themselves to high standards, and we believe that these practices differentiate our members from other providers in the short-term credit industry.

As an economist and lawyer by training, I held several positions in public service and worked in the financial services industry for decades before joining CFSA. My prior work includes serving as Chief Financial Regulator in the state of Ohio, where I helped implement the states first consumer protection laws. Additionally, I served two assignments as a senior advisor to Rep. Barney Frank (D-MA). During that time, I was part of the drafting of the legislation leading to The Dodd–Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), which was created partly in response to the 2007-2008 financial crisis. I supported the creation of the CFPB, and over the past few years have been eager to collaborate with the Bureau to jointly work together in determining what are the best possible consumer protections for our customers.

However, I have often been disappointed by recent actions of the CFPB. Federal legislation that was intended to reform Wall Street has instead been interpreted by the Bureau in ways never intended by Congress — to the detriment ofconsumers. A law that was meant to improve accountability and transparency in the financial system and protect consumers is now being implemented in ways that are anything but transparent. Instead, the CFPB is using suspect and biased data and unpublished research products to support presumptive claims against disfavored nonbank financial products. Most concerning of all, the welfare of consumers does not appear to be the primary concern in CFPB's policymaking. The CFPB has proposed policy options that do not take into account the consequences they will have on consumers' ability to access to credit.

In observing how the CFPB implements the Dodd-Frank Act, I am concerned that the Bureau has at times shown disregard for specific parameters laid out by Congress in the law. Specifically, the CFPB has shown no concern for the devastating impacts in its recent proposal for new rules covering payday lenders, vehicle title lenders, installment lenders and others will have on small businesses. This attitude is evident in the review of the proposal under the Small Business Regulatory Enforcement Fairness Act (SBREFA).[1] Furthermore, the CFPB has failed to follow the text in the statute and has overreached into areas not ever intended by the Dodd-Frank Act. For instance, Congress specifically prescribed into law that the CFPB has rulemaking authority over payday lending, yet the CFPB has combined its proposal forpayday loans with selected other products, such as title and installmant loans, while at the same time, ignoring

[1] Section 1100 G of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 2112 (July 21, 2010).

other like-products such as credit cards and overdraft products.[2] The CFPB has done this without producing any objective, empirical research or information explaining how consumers may use these products separately or interchangeably. In fact the CFPB proposal does not provide any research about how the proposal would impact small businesses. It appears that the CFPB is ignoring the Dodd-Frank Act's mandate to treat like products similarly, while instead picking winners and losers in the financial services marketplace.[3]

## II. Consumers Choose and Appreciate the Payday Loan Product

The 2013 Federal Deposit Insurance Corporation (FDIC) National Survey of Unbanked and Underbanked Households found that 20 percent of U.S. households, or 24.8 million Americans, were underbanked in 2013, meaning that they had a bank account but also used alternative financial services (AFS) outside of the banking system.[4] These recent figures highlight the incontrovertible need for nonbank credit alternatives to serve the millions of consumers using these products.

Our customers know their budgets, and often use the credit provided to them to stay afloat between paychecks. Research from Columbia law school shows that consumers understand the product and can accurately predict how long it will take them to repay their loan.[5] Our customers often use a short-term loan to manage existing debt, such as to pay their utility bills or rent. According to Clarity Services Inc., 89 percent of the time, customer loan proceeds are used for a debt transfer rather than for a new debt. Quite simply, more often than not, the payday loan product is our customers' best or only option, and it is the customer who is best-positioned to know the type of credit that is suitable for their needs.

CFSA is proud of the fact that our customers value our product, and that they like and appreciate our store employees and managers. In fact, a recent survey of payday loan customers conducted by the international polling company, Harris Interactive, found that an overwhelming majority of borrowers are very satisfied or satisfied with their recent payday loan experience (91 percent), carefully weighed the risks and benefits before taking out a loan (93 percent), and value having the option to take a payday loan (95 percent).[6]

One of our biggest disappointments about the CFPB's lack of understanding and proper analysis of payday loan products is that our customers and employees are so often the ones without a voice in the debate. The comments and questions in support of our product from the dozens of customers and employees who have attended CFPB field hearings frequently go unanswered

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[2] Section 1024(a)(1)(E) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 2112 (July 21, 2010).

[3] Section 1033 (e)(1) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 2112 (July 21, 2010).

[4] Federal Deposit Insurance Corporation,"2013 FDIC National Survey of Unbanked and Underbanked Households," October 2014.

[5] Mann, R. (2013). "Assessing the Optimism of Payday Loan Borrowers." Columbia Law and Economics Working Paper No. 443, available at http://ssrn.com/abstract=2232954.

[6] Harris Interactive (2013) "Payday Loans and the Borrower," available at http://cfsaa.com/about-the-payday-advance-industry/survey-payday-loans-and-the-borrower-experience.aspx.

and unrecognized during CFPB policymaking. Attached is a sample of just some of the thousands of positive customer testimonials we have received.

For example, at the recent CFPB Field Hearing on payday lending in Richmond, Virginia, a customer named Shirley talked about her service as a state employee for 46 years and her appreciation for the payday product. Shirley stated that payday loans have been there for people she knows who needed help with healthcare costs, foreclosure costs, and in general when a credit score has precluded them from receiving a bank loan. Shirley stated at the hearing, "I just want to let everybody know that it's the greatest thing that could have ever happened to help people." Shirley was joined at the Richmond hearing by hundreds of other supporters of the product and more than 30 of them spoke positively about payday loan products during the audience participation portion of the hearing.

Despite the CFPB's presumptions that payday loan products harm consumers, the CFPB has produced no evidence to prove this. Instead, the CFPB relies on third-party studies that lack empirical, objective rigor, causing it to draw subjective conclusions. In fact, the vast majority of consumers have favorable outcomes from their use of small-dollar, short-term credit. Research has proven that consumers actually experience positive outcomes as a result of payday loans such as an increase in their credit scores.[7]

Despite the CFPB's claims that payday loans harm consumers, payday loan products continues to have a proportionately miniscule percentage of complaints compared to other types of products. According to the FTC's annual consumer complaint report in 2012, less than one percent of complaints in the "Banks and Lenders" category were about payday loans.[8] Even within the CFPB's own complaint data, it is clear that our businesses have far fewer complaints than those businesses of other financial products and services. In 2014 payday loans accounted for only one percent of complaints, and only one-tenth of those complaints were about storefront lenders.[9] In the CFPB's latest report released last month, once again payday loan complaints remain proportionately much lower than most other products and services, and this is also consistent with a continuously low number of complaints at the state level.[10]

### III. CFPB's Payday Lending Proposal Outline for Small Businesses

On March 26, 2015, the CFPB announced it was considering proposing rules for payday, vehicle title, and similar loans and released a package of materials that outlines the proposals under consideration and alternatives that have been considered. At the same time, the Bureau published an outline of the proposals under consideration in preparation for convening a Small Business Review Panel under SBREFA to gather feedback from small lenders.

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[7] *See* Priestley, J. (2014). "Payday Loan Rollovers and Consumer Welfare." available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2534628.; and Mann, R. (2015). "Do Defaults on Payday Loans Matter?" available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2560005.

[8] Federal Trade Commission, "Consumer Sentinel Network Data Book for January - December 2012" (February 2013).

[9] Consumer Response: A snapshot of Complaints Received, available at http://files.consumerfinance.gov/f/201407_cfpb_report_consumer-complaint-snapshot.pdf (July 2014).

[10] Consumer Response: A snapshot of Complaints Received, available at http://files.consumerfinance.gov/f/201503_cfpb_consumer-response-annual-report-2014.pdf (March 2015).

### A. About SBREFA

Federal law requires federal agencies to evaluate the impacts of their proposed regulations on small entities, to consider alternatives that meet the regulatory goal while minimizing harm to small businesses, and to make the analysis available for public comment. The SBREFA also requires the Environmental Protection Agency, the Occupational Safety and Health Administration, and the CFPB to convene a review panel if the agency finds its proposed rule is likely to have a significant impact on a substantial number of small entities. The review panel's purpose is to receive input from entities that will be directly subject to the proposed rule on (1) the proposal's real-world impacts and compliance costs, and (2) any potential alternatives that would be less burdensome or costly while still accomplishing the agency's regulatory objectives.

A review panel convened under SBREFA consists of representatives from the CFPB, the Office of Advocacy of the Small Business Administration (SBA), and the Office of Information and Regulatory Affairs in the Office of Management and Budget. These agency officials meet with 15-25 individuals selected by the CFPB (called small entity representatives), in consultation with the SBA, for a dialogue about the effects of the potential rule and to explore alternatives that meet the regulatory objectives while minimizing harm to small business operators. After the SBREFA panel convenes, the CFPB prepares a report in the next 60 days with the findings from the panel, including responses to the comments of the small entity representatives.

### B. CFSA Concerns for Small Business Owners and their Families

A central concern for the industry is the unprecedented impact the CFPB's proposal will have on small business owners, their employees, and customers. Within the SBREFA materials released, the CFPB acknowledges that its proposal would sharply reduce revenue for small businesses – and in our estimation would lead to the near annihilation of all small businesses in this industry. In its report the CFPB admits that small businesses will lose 69 to 84 percent of their loan volume, and we believe this is an underestimation.[11]

It is virtually unparalleled for an agency to openly indicate that there will be such a catastrophic impact on small businesses in a SBREFA proposal, and it gives us great concern that there is a lack of consideration for the many employees who will lose their jobs and their source of income. Throughout discussions and in the proposal the CFPB talks about industry "consolidation" which of course is a cleansed way of saying closing businesses. The CFPB even states, "Given those impacts, it is likely the case that the number of monoline stores that could operate profitably within a given geographic market would decrease. Some stores might diversify their product offerings, including offering other forms of covered loans, while others might

[11] Consumer Financial Protection Bureau, "Small Business Advisory Review Panel For Potential Rulemakings for Payday, Vehicle Title, and Similar Loans Outline of Proposals Under Consideration and Alternatives Considered," at p.45, available at http://files.consumerfinance.gov/f/201503_cfpb_outline-of-the-proposals-from-small-business-review-panel.pdf.

close. The proposals under consideration could, therefore, lead to substantial consolidation in the short-term payday and vehicle title lending market." [Proposal, pp. 45-46.]

Despite these sweeping statements and the dismissive references to harming small businesses, the CFPB indicates that it has failed to provide data from actual small businesses in developing the proposal. What data it has provided is based on large businesses and understates the adverse impacts on small lenders. It has also failed to analyze the impacts for each of the product lines that will be regulated.

There is no question that if implemented, the CFPB's proposal will lead to thousands of employees losing their jobs, health benefits, and the ability to support their families. Furthermore, there is no doubt that if the CFPB's proposal were to be finalized as proposed this would create a new adverse precedent for limiting access to consumer credit, ignoring the impact on middle class families and small business owners in the country.

## IV. Limiting Access Will Hurt Consumers

There has been an abundance of research showing that when consumers' access to payday credit is limited, consumers do not stop borrowing; they switch to inferior substitute forms of credit – often products that are unlicensed, unregulated, and offshore.[12] Additionally, research shows that states that have banned payday lending have found that consumers end up worse off.[13] There is ample evidence that restricting access to payday loans may be counterproductive and harmful to consumers. It is imperative for the CFPB to conduct research and analysis about how consumers' welfare will be impacted by its proposal, and it must provide a more detailed cost-benefit analysis before moving forward with the current proposal.

CFSA recognizes that payday loans are just one of many tools in a consumer's financial toolbox, albeit a critically important one. As a Federal Reserve Board economist and his colleagues found, "initial payday loan applications occur precisely when consumers' access to liquidity from mainstream creditors is lowest."[14] Despite some good intentions, many opponents of our industry have supported restrictions that in reality leave the consumer worse off, and with less choice rather than more.

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[12] *See* Goldin, J. and Homonoff, T. (2013). "Consumer borrowing after payday loan bans." available at http://scholar.princeton.edu/jgoldin/publications/consumer-borrowing-after-payday-loanbansReport_2670FS.pdf.); and Morgan, D.P., and Strain, M.R. (2008). "Payday Holiday: How Households Fare after Payday Credit Bans." Federal Reserve Bank of New York Staff Reports, no. 309, available at http://www.newyorkfed.org/research/staff_reports/sr309.pdf.)

[13] *See* Morgan, D.P., and Strain, M.R. (2008). "Payday Holiday: How Households Fare after Payday Credit Bans." Federal Reserve Bank of New York Staff Reports, no. 309, available at http://www.newyorkfed.org/research/staff_reports/sr309.pdf; Zinman, Jonathan (2009) "Restricting Consumer Credit Access: Household Survey Evidence on Effects Around the Oregon Rate Cap" available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1335438; and Desai, Chintal and Ellihausen, Gregory (2013) "The effect of state legislation restricting payday lending on consumer credit delinquencies: An investigation of the debt trap hypothesis" available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2418608.

[14] Bhutta, N.; Skiba, P.M.; and Tobacman, J. "Payday Loan Choices and Consequences," Vanderbilt University Law School Law & Economics Working Paper Number 12 – 30, January 25, 2013.

CFSA strongly opposes the numerous presumptions and conclusions drawn in CFPB's proposals, which do not have any basis in research or data. We urge the CFPB to start over again and work with us to better understand our small businesses, their employees, and the needs of our customers. The CFPB and consumers would both be better off if the Bureau begins a regulatory process properly equipped with research and data and an informed understanding of how consumers use our products.

In conclusion, we are fearful that the CFPB's proposal is unduly burdensome on small businesses and will create job loss and financial instability for American families. Furthermore, the proposal would restrict access to credit for consumers, and limit the ability of our members to offer their products to families in their community. In turn, this would force consumers to turn to unsafe, unregulated and unlicensed forms of credit.

CFSA looks forward to working with Congress to help protect the livelihood of our small business owners who reside, and provide employment opportunities, in many of your districts. Thank you for inviting me here to testify today.

***Customer #1 (from Alabama)***
**CFPB Payday Lending Field Hearing**
**January 19, 2012**
***Short-term credit customer (public testimony)***
https://youtu.be/C2UlSsmHISI?t=1h46m29s
**Name: LaDonna Banks**
"Hello, my name is LaDonna Banks, and, I'm here on behalf of, actually needing a payday loan at one time. And when the gentleman said it has a lot to do with education or lack of that's not true. My situation was an emergency situation. I had a brother on life support that was very sick and needed a kidney and preparing and preplanning was not an option. Donating my kidney was and that's what I did. I donated the kidney to my brother and then the process for waiting for my short-term disability to kick in, I had a bridge of two and a half weeks that I had to get money in order to keep from getting $210 in bank fees. I borrowed the money. I paid the money back in two weeks. It was perfectly fine, and it was a need and a necessity for me at that time."

***Customer #2 (from Arizona)***
"I came in for a short term loans because my car broke down & Vanessa and Linda was a tremendous help. This allowed me the opportunity to get my car fixed so that I may continue with me business."

***Customer #3 (from California)***
"Short term loan has helped on a couple occasions. Short notice car repairs in order to keep vehicle running to get to work. Also during a medical emergency to allow wife to go to the hospital downstate with our daughter."

***Customer #4 (from California)***
"Payday loans are good when you are in a bind and need help. It's better than paying an overcharge fees the bank charges on every item you are overdrawn."

***Customer #5 (from California)***
"Payday loans have helped me with emergencies, like prescriptions for illness and absolutely do not have any cash. It could mean life or death in some circumstances pharmacies do not give free medicine"

***Customer #6 (from California)***
"It really helps to be able to get a loan when one cannot get one through a banking institution. I needed my truck repaired and would not have been able to if it had not been for the payday loan."
***Customer #7 (from Florida)***
"The cash advance has been a huge help for me when I'm short on getting a bill paid like my water, electric and insurance payments. I use to be late on my bills when that happens but now with the cash advance, that never happens and I've saved a lot of money avoiding late fees."

***Customer #8 (from Florida)***
"If ever I'm late on any of my bills like my electric bill, the cash advance is my best option in getting it paid fast so it doesn't get shut off. This helps us not to overdraw our bank account to it saves us from any kind of overdraft."

***Customer #9 (from Florida)***
"I'm self employed and sometimes I have to wait to be paid by my customers and the cash advance at times will help me get by while I'm waiting for those checks to come in. So at this time this our only option to help us out when we need it."

***Customer #10 (from Florida)***
"I use the cash advance for pretty much everything whenever I need cash quick. It's primar used for when I have something due and it is due just before I get paid. If it weren't for this my late charges would be out the roof."

***Customer #11 (from Florida)***
"Being a single person the cash advance is my back up plan when I'm short on getting something paid or if I have and emergency that comes and I need some help. This keeps me from having to go to a family member or worse...pay late fees."

***Customer #12 (from Florida)***
"The cash advance gives me time to get my bills paid before my next monthly check comes in. The piece of mind is priceless. I much prefer using this service instead of putting things on my credit card where I may only make the minimum payments. So it forces me to say on top of my bills."

***Customer #13 (from Florida)***
"The only thing I use the cash advance for is to help me out with my bills when I run short durring a particular month. I don't really have a any other alternative due to my credit and the pawn shop is out of the question because of their high rates."

***Customer #14 (from Florida)***
"I use the cash advance to make sure that I don't over draft my checking account because if I bounce a check it would cost $35. It's hard being a single mom and I have to keep up with my bills so this is my best avenue to get just a little bit of cash to put me over the edge."

***Customer #15 (from Florida)***
"Whenever I need some help because I'm short on a bill I use the cash advance to help me get it paid on time because the late fees are way more that what a cash advance costs. I don't have any idea what I would do without it. I would be late on so many bills and the late fees would pile up to the point that I would be even further behind."

***Customer #16 (from Kansas)***
"[payday loans] this helps in a lot of different ways. Interest rate is bad, but no worse than credit cards. What happened to free enterprise."

***Customer #17 (from Kansas)***
"We do not have credit cards nor do we wany any. So if we have unexpected expenses like car repairs or doctor bills, it is nice to know we don't have to risk not paying a bill or rent. We would have not survived very easily these past few years w/o payday loans. When used responsibly they are a good thing."

***Customer #18 (from Kentucky)***
"On behalf of everyone thank you for doing business with my family at the time of are needs includes the following excellent service your company provides in a friendly and professional environment.

It enabled me to unexpected repairs on home due to the weather.

I am retired on monthly income and sometimes I might need a computer or printer

For my business, so it is handy to have your company nearby.

Please represent my right to choose which financial option makes the best sense for me."

***Customer #19 (from Tennessee)***
"The payday loan I received helped me not to default on a bill during a time when my income had been cut. When my pay got back to normal I then payed off my payday loan. I believe that payday loans supply useful need in our society."

***Customer #20 (from Tennessee)***
"Do to my poor credit score I am not able to get a traditional credit line. This allows me to get the cash I need in order to pay for gas I need to operate a gas station auditing route."

***Customer #21 (from Tennessee)***
"Overdrafted on account accidentally. Provided me ability to keep from paying added fees."

***Customer #22 (from Tennessee)***
**CFPB Payday Lending Field Hearing**
**March 25, 2014**
***Short-term credit customer (public testimony)***
https://youtu.be/ZpnXG0UdeoQ?t=2h16m4s
**Name: Jeanine**
"Hello, I'm a payday loan consumer and have been for probably 10 or 12 years. And, um, I'd like to say it's always been extremely clear what the cost is of borrowing that money is. It can't be much simpler than you're going to borrow $200 and you're going to pay back $230. Um, I feel more abused by the banking industry who if I overdraft my bank account by $1 they'll charge me $35. I heard people talk about 400 percent interest, I'm pretty good with math but I can't even tell you what that interest rate would be. Um, nobody's talked about, you know the family who can't pay the electric bill. When the electricity bill gets turned off, they're going to be charged $150 to turn it back on. Um, nobody's concerned about those fees. And these are the kinds of things that I've had a payday loan work for me over the years. I've always know that I could rewrite that loan at a lower amount each time to pay it off if I couldn't pay it off in full. And I found that the people that work in the payday loan stores to be above and beyond to explain to me what I'm paying for the service they're giving and what other services they have available. Cause it isn't a one-size-fits-all. And they do have more than one product depending on what the situation might be for the consumer. So I think it would be a real disservice to the people who don't have real access to a pocket full of credit cards or a banker they can call for a personal loan to try to limit this industry. Because those are the people who need this service the most…"

***Customer #23 (from Utah)***
"Since my husband got sick and I am having to work 2 jobs, sometimes it's the only way to make it to the next paycheck. I get just enough to get the medicine my husband needs and to put food on the table. It works for me."

***Customer #24 (from Utah)***
"My son fell off our porch and received a head injury. He was life flighted to Primary Children's Hospital. I had to pay a co pay of 200. My payday loan allowed me to do this and still pay my regular bills."

***Customer #25 (from Virginia)***
**CFPB Payday Lending Field Hearing**
**March 26, 2015**
***Short-term credit customer (public testimony)***
https://youtu.be/a8f2700SilY?t=9s
**Name:** Elvin
"Hi my name is Elvin. I'm a satisfied customer with Check City. I've been retired for 17 years. I've been banking with a credit union for 44 years, and when I had problems they wouldn't even give me a loan. And I'm still a customer of the credit union since 1970. So every now and then I went in to … it's been six years and

I'm satisfied with everything that I get. When I need, all I have to do is go in there and talk to them. But they look at my application and look at my salary and after I sign all the papers about military. And every time they give me a short-term loan. I understand it. And that's the way I go. But in regular financial institutions they are not their brother's keeper and all ya'll know that. And I think ya'll need to get on these people that buy this debt, and do all this crazy stuff. I don't know if it's the payday loans themselves but it's the people they sell the debt to that do all this stuff. ... but I've been a customer of a credit union for 44 years and when you have a hard time they don't want to talk to ya."

***Customer #26 (from Virginia)***
**CFPB Payday Lending Field Hearing**
**March 26, 2015**
***Short-term credit customer (public testimony)***
https://youtu.be/lp4Tpin55wo?t=45m18s
**Name:** Miss Shirley
"Hello everyone, my name is Shirley. I've been at my job for 46 years with the state. But that's irrelevant. I just wanted someone to know. Payday loan, title loan, and any other kind of loan that you can get, where you don't have to worry about going into a bank and they telling you 600 and all this about a credit report when you done did 50 years and 30 years on paying a mortgage. What do you think about that? When the other thing was excellent, and everything was paid. Nobody get the credit. I have a cousin, who if it wasn't for a payday loan she'd be dead. That's right, it's taken care of her chemo. Took care of my best friend's foreclosure. Where was the bank back then? And that girl did 30 years with the state. When you got to go into a bank and you gotta care about your credit ...what about my credit. My credit is awesome. And I thank God. But I just want to let everybody know that it's the greatest thing that could have ever happen to help people..."

***Customer #27 (from Virginia)***
"[payday loan] It assisted me with repairs to my vehicles. I'm a business owner of a transportation service. It provided funds to do repairs in a timely manner. This allowed me to continue with my services to the customers. I service for employment purposes."

***Customer #28 (from Washington)***
"Moneytree is very convenient, easy, fast – don't have to sit there and wait for days waiting to find out - like at a bank. The branch in Port Orchard is fantastic – I imagine the rest of them are the same way.
I know that if there is a situation, I don't have to wait for a FICO score or the embarrassment of not getting it from a bank. A tire's blown the kid needs something for school tomorrow – you've got a payday loan. It's for people who need the cash now, and can't afford the time or time away from work to get a loan from a bank.

I know the government wants to limit the number of loans we can take – but real life just happens. Unfortunately it happens. You pay one bill and then the water heater goes out. They don't want to wait to get paid. The government forgets about people that don't have the great credit scores. You're showing that you can pay stuff back – and you get the water heater repaired, new shoes for the kids to go to school in and you get it done.

They have limited the ability for myself and others to get the short term loans by limiting the number you can take. Real life happens. Banks limit and bases it all on a credit score – and that hurts everyone. It hurts the banks, it hurts consumers and it drives people to payday lenders. But I use these products because it's convenient. If I'm short on money for groceries – it's right there. It's convenient."

**Testimony of Mitria Wilson**

Vice President of Government Affairs and Senior Counsel,
Center for Responsible Lending

Before the U.S. House Committee on Financial Services'

Subcommittee on Financial Institutions and Consumer Credit

**Examining Regulatory Burdens on Non-Depository Financial Institutions**

April 15, 2015

Good afternoon Chairman Neugebauer, Ranking Member Clay, and Members of the House Committee on Financial Services' Subcommittee on Financial Institutions and Consumer Credit. Thank you for allowing me to testify about the regulatory burdens on non-depository financial institutions and the need to ensure that all financial institutions, both depository and non-depository alike, are subjected to responsible regulatory oversight that maintains sensible consumer protections.

I am the Vice President of Government Affairs and Senior Counsel at the Center for Responsible Lending (CRL). CRL is a nonprofit, non-partisan research and policy organization dedicated to eliminating abusive financial practices, while protecting homeownership and family wealth. As an affiliate of Self-Help, a nonprofit community development financial institution, CRL's research and policy positions are informed by the business reality and experiences of a community lender. For thirty years, Self-Help has built a small, community-based financial services institution that focuses on creating asset-building opportunities for low- and moderate-income, rural, women-headed, and minority families. In total, Self-Help has provided more than $6 billion in financing to 70,000 homebuyers, small businesses, and nonprofits and currently serves more than 80,000 mostly low-income families through 30 retail, credit-union branches in North Carolina, California, and Illinois. The business success of Self-Help reassures CRL's confidence in the fact that responsible regulations and regulatory oversight are core to all consumer lending.

In the invitation to testify, the Subcommittee on Consumer Credit and Financial Institutions requested that witness testimony "provide an overview of the current regulatory climate and how it affects the ability of community financial institutions to provide financial

services or products to consumers." Accordingly, this written testimony proceeds in five parts. **Part 1** of the testimony will provide an overview of the importance of financial regulations and the current role that they play in protecting consumers, taxpayers, and the nation's economy as whole. In the remaining portions of the testimony, CRL focuses on discussing and providing specific policy recommendations on the regulatory environments for non-depository financial institutions that provide four types of consumer products and services:

**Part II** focuses on non-depository institutions that provide mortgage loans;

**Part III** focuses on the regulation of title insurance for mortgaged properties;

**Part IV** focuses on payday and car-title loan products; and

**Part V** focuses on the regulation of indirect automobile lenders.

Our conclusion is that important distinctions in the business models and practices of non-depository institutions in each one of these product sectors ultimately justifies increased federal regulatory oversight of consumer protections.

## I. Recent history and the current market environment proves that financial regulations are critical.

As we engage in a national conversation about the regulatory burdens facing the financial services sector, it is important for policymakers to remember why financial regulations are essential to preserving the health of this nation's economy. Done correctly, responsible financial regulations are a good thing. They protect consumers from abusive and harmful financial products, ensure the safety and soundness of financial institutions, and prevent systemic risk from threatening to undermine the nation's financial market as a whole.

Recent history has already shown us the consequences of under regulation in the financial market. In the wake of the financial crisis, 5.5 million American consumers lost their homes

through foreclosure; unfortunately, that number continues to grow.[1] And, according to the Federal Deposit Insurance Corporation, more than 500 banks shuttered their doors, with most of those institutions being community banks.[2] The failure to have a responsible regulatory environment also resulted in taxpayers paying $7 trillion to bail out financial institutions through loans and, according to some reports, an additional $22 trillion through the federal government's purchase of assets.[3] In addition, the national economy was undermined and plunged into a severe recession. To put it bluntly, people lost their jobs, small businesses went under, and many Americans—from small entrepreneurs to families—struggled to make ends meet while being unable to obtain the credit and capital they needed from financial institutions in order to sustain their position or expand their asset base.

The negative nature of these consequences makes one thing clear:

> ***Proactive, responsible financial regulations—like those being enacted under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank)[4]—are both necessary and key to protecting consumers, small businesses, taxpayers, and the nation's economy overall.***

And it is equally clear that oversight is necessary for every actor in the financial market, whether they are as large as J.P. Morgan Chase, a mid-size regional institution, a community bank lender or credit union like CRL's affiliate, Self-Help, or a non-depository lender like Freedom Mortgage, Advance America, and First American Title Insurance Company. All financial institutions—including non-depositories—benefit from the underlying purposes of financial regulation: protecting consumers, ensuring the safety and soundness of these institutions,

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[1] Corelogic, "CoreLogic Reports 41,000 Completed Foreclosures in November 2014," (January 14, 2015) *accessed at* http://investor.corelogic.com/mobile.view?c=118425&v=203&d=1&id=2007499.
[2] Federal Deposit Insurance Corporation, *Failed Bank List*, *accessed at* https://www.fdic.gov/bank/individual/failed/banklist.html
[3] John Carney, "The Size of the Bank Bailout: $29 Trillion," *CNBC*, December 14, 2011, accessed at http://www.cnbc.com/id/45674390#.
[4] Public Law 111-203 (2010).

preventing unfair competition, and defending the nation's financial market from systemic risk. The question is whether there are different, more effective ways to ensure that these objectives are being met when regulating non-depositories.

For a myriad of reasons, discussed in further detail below, the business models and market realities of non-depository institutions are very different than their community-based, depository counterparts. These differences justify increased federal regulatory scrutiny of non-depository business practices in providing consumer financial products and services.

## II. Recommendations concerning the regulatory environment for non-depository mortgage lenders.

A recent opinion editorial in American Banker asserted that Congress's regulatory relief efforts were ignoring "the regulatory burden on small and mid-size, community-based, non-depository mortgage lenders."[5] Yet, that same editorial overlooks some very important distinctions between the mortgage business models of depository and non-depository lenders.

Community-based depository lenders and credit unions, and the financial services that they provide, are both important and distinctive. CRL appreciates that small, depository lenders and credit unions frequently use a business model to provide financial services to consumers that often involve smaller transactions and is based on the institution having much closer ties to both the borrowers and communities that they serve. The result is a tailored lending and underwriting process that can produce more successful mortgage lending and has a track record that demonstrates that success. Also, unlike their larger bank counterparts, smaller depository

[5] *See* Paulina McGrath, "*Little Relief for Nonbank Mortgage Lenders*," American Banker (April 13, 2015).

financial institutions are less likely to participate in capital market transactions. Previous testimony from industry organizations, like the American Bankers Association and the Independent Community Bankers of America, has shown that community banks oversee a much smaller percentage of the nation's financial assets—on average less than $1 billion at each institution—and operate with far fewer employees, with industry estimates ranging from staff averages of 40 to 54.[6]

In contrast, non-depository mortgage lenders are rarely community based. Rather than using a lending model that depends on a long-standing business relationship with a consumer and actual ties to the community that they live in, non-depository mortgage lenders often engage in a single interaction with a consumer that lives in a community where the non-depository lender has no brick and mortar presence. For example, Freedom Mortgage—one of the most visible non-depository providers of FHA, VA, and USDA guaranteed mortgage loans—is licensed to operate in all 50 states, but it serves consumers on a national basis while maintaining a physical presence in just 8 locations: New Jersey, California, Arizona, Minnesota, Illinois, Indiana, Delaware, and Florida.[7] Most community bank lenders would take exception to the claim that Freedom Mortgage's New Jersey-based office was engaging in community-based lending in Texas just by making a single mortgage loan to a consumer located in Houston. In considering regulatory relief for community-based, financial institutions, we must ensure that the institutions we provide that relief to are legitimately community-based. There is little evidence that non-depository mortgage lenders satisfy that requirement.

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[6] Mr. Jeff Plagge, American Bankers Association, Hearing before the Senate Committee on Banking, Housing, and Urban Affairs, *Examining the State of Small Depository Institutions*, 113th Cong. 2d sess, 2014; Mr. Jeff Plagge, Independent Community Bankers of America, Hearing before the Senate Committee on Banking, Housing, and Urban Affairs, *Examining the State of Small Depository Institutions*, 113th Cong. 2d sess, 2014;

[7] *See* https://www.freedommortgage.com (last accessed on April 13, 2015).

There are also other distinctions that suggest that the regulatory environment for non-depository mortgage lenders should differ from the environment for small, community-based, depository lenders. For example, while community bank staff averages range from 40 to 54 employees, the Community Mortgage Lenders of America notes that the average independent mortgage banker can have staff up to 250 employees.[8] Those numbers suggest that the compliance burden is less for non-depository lenders.

Moreover, a key component of the rationale for providing regulatory relief to community-based, depository mortgage lenders rests on the recognition that these lenders do not engage in significant capital market transactions and often retain mortgage loans in their portfolios. In contrast, non-depository mortgage lenders "do not have a loan portfolio and have no access to bank deposits to fund their operations and no access to the Federal Reserve window for liquidity."[9] Thus, their business model depends upon originating to sell mortgage loans in the capital market.

Proponents of regulatory relief for non-depository mortgage lenders suggest that the personal guarantees of independent mortgage lenders and "the fact that their own net worth is almost always tied up in their company," should be enough to mitigate against the fact that their originate-to-sell business model means that they have little or no risk if the loans they originate perform poorly.[10] But experience casts doubt on the strength of this assertion.

A report by the Center for Public Integrity found that, just five years after housing market's crash, top executives from the 25 largest and most problematic lenders were back in

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[8] *See* Paulina McGrath, "*Little Relief for Nonbank Mortgage Lenders*," American Banker (April 13, 2015).
[9] *Id.*
[10] *Id.*

business as non-depository mortgage lenders. 14 of those executives were the founders or CEOs of companies that previously failed due to risky, predatory lending.[11]

Given the differences in business practices, company resources, and track records, CRL supports a regulatory framework and oversight structure that appropriately recognizes and accommodates the unique nature of community bank and credit union mortgage lenders, while employing an approach toward non-depository mortgage lenders that recognizes that they are, in fact, different. Because their business model is more closely aligned with the practices of larger, depository institutions, non-depository mortgage lenders should be subjected to the same level of scrutiny as other financial institutions that employ an originate-to-sell model.

Nearly 9 out of 10 mortgages in the United States are made by noncommunity bank lenders.[12] Substantive rollbacks of Dodd-Frank's mortgage provisions with broad applicability undermine Dodd-Frank's goal of protecting consumers as a whole and preventing the recurrence of another foreclosure crisis. Rollbacks should not be included in community bank regulatory relief legislation. Moreover, it is important that regulators understand how non-depository mortgage institutions work and take those factors into account when regulating. During the crisis, non-bank mortgage lenders were responsible for some of the most problematic and predatory mortgage products that were issued to consumers and then sold to investors on the secondary market.[13] CRL believes that loosening consumer protection requirements for these institutions in the name of regulatory relief could invite the return of unsustainable mortgage lending.

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[11] Daniel Wagner, "*Subprime lending execs back in business five years after crash*," Center for Public Integrity, September 11, 2013 (accessed at http://www.publicintegrity.org/2013/09/11/13327/subprime-lending-execs-back-business-five-years-after-crash on April 11, 2015).
[12] Federal Deposit Insurance Corporation, *Statistics on Depository Institutions*.
[13] *See* Robert Kolb, *Lessons from the Financial Crisis: Causes, Consequences, and Our Economic Future*, at 563 (John Wiley & Sons 2010).

Instead, the focus should be on what will help traditional community banks and credit unions, while protecting consumers, the institutions, and the nation's economy as a whole. Thankfully, the Consumer Financial Protection Bureau, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, and National Credit Union Administration have been mindful of the differences between larger institutions and smaller lenders and are working to tailor rules implementing Dodd-Frank accordingly.

The CFPB, in particular, has developed a successful track record in taking the lead to adopt and consider regulations that are balanced for financial institutions and accommodate smaller lenders. For example, the CFPB recently requested comment on whether to increase the 500 first-lien mortgage cap under QM's small-creditor definition. CRL expressed support for a reasonable increase of the 500 loan cap, limiting any potential increase to rural banks or for loans held in portfolio. The CFPB's proposal quadruples the limit, expanding the loan origination cap for small lenders from 500 first-lien mortgages to 2,000. This 2,000 limit is exclusive of loans held in portfolio by both the creditor and its affiliates.

The CFPB has also proposed to only include first-lien mortgage originations of small lender and its affiliate assets towards the current $2 billion asset cap. And, to accommodate concerns that the definition of a "rural and underserved" area is too narrow, the CFPB has proposed expanding the definition of rural areas by including census blocks as defined by the Census Bureau. Finally, the CFPB is also proposing to allow grace and qualifying periods for small creditors to adjust to current and proposed standards. While we may not always agree on all specifications, we have and continue to support the CFPB's ongoing efforts to reasonably explore how mortgage rules can further accommodate small lenders and lending in designated rural and underserved areas.

In addition to the CFPB's activity with mortgage rules, financial regulators are working with industry, consumer groups, and other stakeholders to review their regulatory framework, as required by the Economic Growth and Regulatory Paperwork Reduction Act of 1996.[14] Under the existing law, the agencies must eliminate any unnecessary regulations and are required to report their actions to Congress next year.

Finally, regulators have reported that technical assistance and ombudsman programs have been extremely effective vehicles for providing regulatory assistance to community banks and credit unions. The effectiveness of these programs, however, depends upon adequate funding. CRL recommends that any regulatory relief legislation include increased funding for regulators' technical assistance and ombudsman activities.

## III. Recommendations on the regulation of title insurance for mortgaged properties.

The Consumer Financial Protection's correctly decided to include affiliated title insurance fees within the cap on points and fees in the qualified mortgage definition component of the ability-to-repay rule. Proposals to exempt affiliated title insurance from the Qualified Mortgage points and fees limit are costly and unnecessary for borrowers. We are concerned that, if passed, these proposals will continue to foster an anti-competitive business market in an industry where prices have already proven to be severely inflated.

Title insurance companies are exempt from federal anti-trust laws.[15] The result has been a market where consumers exercise little choice, while paying costs that bear little relation to the actual loss claims that the industry actually experiences. In 2007, a GAO report concluded that borrowers "have little or no influence over the price of title insurance but have little choice but to

[14] Public Law 104-208 (1996), codified at 12 USC §3311.
[15] *See* McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015 (2014).

purchase it." As a result, the fees are grossly inflated. Recent studies have found that 70 cents of every premium dollar for title insurance goes to commissions, whereas 5 cents to 11 cents goes to paying claims.[16]

Anti-competitive practices put companies at a significant disadvantage if they market directly to consumers and can offer lower rates. One such company, Entitle Direct, has roughly .1% of the market, despite the fact that their fees are often 35% less than the competition. One expert explained that the challenge is, "the limited price competition in title insurance markets and the strength of the institutional arrangements between title insurers and those able to steer title business — lenders, developers, realtors, and builders.".[17]

Excluding affiliated title insurance costs from the points and fees cap is especially inappropriate given the limited state or alternative federal oversight of the title insurance industry. A 2010 study from the National Association of Insurance Commissioners regarding state regulation of title insurance reports that half of all states either do not regulate title insurance rates or allow insurers to set their rates and essentially notify the regulators.[18] Only a handful of states adequately review rates to prevent price gouging, while nearly half have "file and use" or "use and file rules."[19] In these states, insurer rate schedules automatically go into effect after a specified number of days unless the regulator intervenes. In many of these

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[16] U.S. GOVERNMENT ACCOUNTABILITY OFFICE, TITLE INSURANCE: ACTIONS NEEDED TO IMPROVE OVERSIGHT OF THE TITLE INDUSTRY AND BETTER PROTECT CONSUMERS 53 (2007), *available at* http://www.gao.gov/new.items/d07401.pdf.
[17] Lisa Prevost, Saving on Title Insurance, New York Times (March 14, 2013), *available at* http://www.nytimes.com/2013/03/17/realestate/saving-money-on-title-insurance.html?_r=0.
[18] NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS TITLE TASK FORCE, SURVEY OF STATE INSURANCE LAWS REGARDING TITLE DATA AND TITLE MATTERS 8 (2010) *available at* http://www.naic.org/documents/committees_c_title_tf_survey_state_laws.pdf.
[19] *Id.*

instances, the regulator is not required to respond and, in practice, they rarely do. The remaining states only require that the rates be "reasonable," or they fail to regulate title insurance at all.[20]

While the federal Real Estate Settlement Procedures Act (RESPA) prohibits paying kickbacks to third-party title agents, the law does not prohibit payments to affiliated title firms. This omission in the law incentivizes a title agency to be affiliated so that it can collect additional payment without violating RESPA.[21] By including affiliated title costs in the points and fees cap, the CFPB's rulemaking simply levels the playing field between affiliated and unaffiliated title insurance in a way that encourages more competition in the market with more choices and better pricing for consumers.

## IV. Recommendations on the regulatory environment for non-depository providers of payday and car-title loan products.

The history of the regulation of payday lending takes us to the states. Payday loans were legalized only in relatively recent years and only in some states, as the result of payday lenders' pushing for an exception to a state's interest rate limit. The payday lending industry promoted the loan's 300- or 400% annual interest, along with direct access to borrowers' checking accounts or car title, on the premise that the loan was for an emergency, once-in-a-blue-moon situation, and was just a two-week or one-month loan. The data, as we'll look at in a minute, show conclusively that this is not how these loans have operated. As a result, the recent trend has been more states closing these exceptions. Today about a third of states don't permit high-cost payday lending.

So with that context, we turn to the data, which show that the fundamental model for these loans is anything but "once in a blue moon." It really is a debt trap. The Bureau's data show

[20] Joyce D. Palomar, Title Insurance Law: Chapter 18 State Regulation of Title Insurance, 2 Title Ins. Law § 18:17-22 (2014-2015ed.)
[21] 12 U.S.C. 2607(c)(4), as amended.

75% of all payday loans are from borrowers with more than 10 loans per year, with those loans churned on a nearly continual basis. CRL's published research shows that the average payday borrower is in these purportedly two-week or one-month loans for seven months of the year, with the loan being flipped over and over.

This churn evidences the borrower's lack of ability to repay. Since the lender holds the borrower's check or ACH access, and the loan is due on the borrower's payday, most loans are collected. However, the borrower does not have enough money left for necessities like food and housing, and is forced into another loan.

Car title loans operate the same way, with huge harm to borrowers because they often lose their car – undercutting a borrower's ability to get to work and earn an income. Installment loans with direct access to the borrower's account also often operate in this same way, with built in flipping.

Lenders' determining the borrower's ability to repay without re-borrowing is an essential principle of responsible lending. It is practiced and required in other contexts, like mortgage lending. It is especially important for payday loans since the normal incentive to underwrite is flipped on its head: again, these lenders hold direct access to the borrower's checking account, first-in line, so they will usually be repaid, and loan churning —which happens when the borrower cannot afford the loan—produces much of the lenders' revenue.

The Consumer Financial Protection Bureau's proposal notes it is considering providing "options" lenders can choose in lieu of determining ability to repay, for both short-term and longer-term loans. This approach would violate this fundamental, essential ability-to-repay principle and undercut the effectiveness of reform of this lending. Exemptions from determining

ability-to-repay for what are some of the riskiest financial products available—and again, illegal in many states— are totally inappropriate. No loan with these features should ever be exempted from responsible underwriting. And indeed in the mortgage context, the Bureau recognized that a safe harbor was inappropriate for subprime mortgages; it should likewise refuse to sanction a lack of underwriting for these high-risk loans.

In conclusion, the financial prospects of millions of families have been derailed by abusive consumer loans, and effective reform of this market is essential. CRL supports the CFPB's efforts to bring much needed oversight and regulation to the payday and car-title loan industries.

## V. Recommendations on the regulation of indirect automobile lenders.

Automobiles are the most common nonfinancial assets held by American households.[22] For most individuals, car ownership is not a luxury, but a prerequisite to opportunity. Cars not only provide transportation, but also options for where to work and live, and how we interact with our community. As a result, both the affordability and sustainability of auto financing are central concerns for American families.

When a car buyer finances a car through a car dealer, he or she signs a contract with the dealer for the car purchase and loan. In the vast majority of cases, the dealer seeks to quickly sell that contract to a third party, such as a bank or finance company. The potential purchasers of the loan receive the consumer's financial information to help them determine pricing for the loan and to set parameters for the other terms and conditions of the loan. The dealer collects bids from

[22] Federal Reserve Board, *Changes in U.S. Family Finances from 2004-2007: Evidence from the Survey of Consumer Finances*, Feb 2009. Approximately 87.0% of families in the U.S. owned at least one vehicle in 2007.

many interested financial institutions, who outline the terms and conditions they will accept, including the interest rate.

What most car buyers don't know is that the financial institution purchasing the loan provides the dealer discretion to manipulate the interest rate for compensation. For example, a bank may be willing to buy the contract as long as the interest rate is at least 4 percent, but will permit the dealer to add up to 2.5% to the rate and charge the consumer 6.5 percent interest. The dealer receives some or all the difference between the interest rates as compensation.

The Center for Responsible Lending estimates that for consumers who financed cars through a dealer in 2009, buyers will pay $25.8 billion in interest over the lives of their loans solely attributable to this markup.[23] In 2009, for example, CRL's data indicates that the average markup was nearly 2.5 percent, hiking costs for each loan by hundreds of dollars.[24] While we believe dealers should be compensated for the work they do in financing cars, they shouldn't have arbitrary discretion to levy a hidden charge for financing that costs some buyers far more than others.

The markup system persists in spite of a history of legal violations dating back to the late 1990s. Again and again, lawsuits and investigations have found pricing discrimination. Not only do car buyers of color receive interest rate markups more frequently, they also consistently get higher markups than white borrowers with similar income and credit profiles.

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[23] Delvin Davis and Joshua M. Frank, *"UNDER THE HOOD: Auto Loan Interest Rate Hikes Inflate Consumer Costs and Loan Losses,"* at 2, Center for Responsible Lending (April 19, 2011).
[24] *Id.*

Most recently, the Consumer Financial Protection Bureau and the Department of Justice announced a settlement with Ally Financial alleging discriminatory markup practices.[25] The CFPB and DOJ found that the average African-American car buyer who received an Ally loan through the dealer paid more than $300 in additional interest over the course of the loan than white borrowers with similar qualifications. While agreeing to pay $98 million to settle these claims, Ally has also said that it plans to continue granting dealers the discretion to manipulate interest rates for compensation.

The National Automobile Dealers Association recently proposed a voluntary plan for its dealers. Under this plan, rather than increase the interest rate on a case-by-case basis, dealers would mark up every interest rate. But here's the catch: Dealers would still be free to lower rates if they so choose, citing exceptions that would provide virtually unfettered discretion. This means that certain groups of consumers could still find themselves paying unjustifiably higher interest rates.

Dealers justify markups by noting that consumers can negotiate the interest rate on their loan just like on the price of the car. The problem is this: Negotiating the interest rate doesn't always result in better pricing, particularly for certain groups.

A Center for Responsible Lending report shows that even though borrowers of color reported negotiating their interest rates at the same or higher rates than white borrowers, those groups still paid higher interest rates.[26] The data also showed that borrowers of color were more

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[25] *CFPB and DOJ Order Ally to Pay $80 Million to Consumers Harmed by Discriminatory Auto Loan Pricing*, accessed at http://www.consumerfinance.gov/newsroom/cfpb-and-doj-order-ally-to-pay-80-million-to-consumers-harmed-by-discriminatory-auto-loan-pricing/ (last accessed on April 13, 2015).

[26] Delvin Davis, "*Non-Negotiable: Negotiation Doesn't Help African Americans and Latinos on Dealer-Financed Car Loans*," Center for Responsible Lending, January 2014, accessed at http://www.responsiblelending.org/other-consumer-loans/auto-financing/research-analysis/CRL-Auto-Non-Neg-Report.pdf (last accessed April 13, 2015).

likely to be told information leading them to believe that further negotiation would be fruitless. When the dealer leads a consumer to believe that the interest rate is the best that dealer can find--even though that may not be true --the consumer stops negotiating.

Ultimately, the financial institutions that purchase auto loan contracts have the power to stop abusive markup practices, but, as with the dealers, they don't seem to be rushing to change. Recently, Wells Fargo also announced that it will continue to allow dealers to mark up interest rates for compensation.

The Center for Responsible Lending believes that this particular form of compensation, with its' long history of unfairness, should be eliminated. Dealers already get compensated in ways other than marking up the interest rate. For instance, dealers receive a flat fee for every loan made under zero-percent and other low-interest rate promotions that manufacturers may offer. Under a system without dealer pricing discretion, dealers will still get compensated for their work, but with less incentive to sell consumers on the highest interest rate possible.

In 2013, the Consumer Financial Protection Bureau issued a bulletin reminding indirect auto lenders of their compliance responsibilities under the Equal Credit Opportunity Act.[27] That law makes it illegal for a creditor to discriminate in any aspect of a credit transaction on prohibited bases, including race, color, religion, national origin, sex, marital status, and age. The bulletin was meant to clarify the CFPB's authority to pursue auto lenders whose policies can, at times, be used to harm consumers through unlawful discrimination.

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[27] *See* CFPB Bulletin 2013-02, "*Indirect Auto Lending and Compliance with the Equal Credit Opportunity Act*", March 21, 2013, accessed at http://files.consumerfinance.gov/f/201303_cfpb_march_-Auto-Finance-Bulletin.pdf (last accessed April 14, 2015).

The CFPB noted that lender policies that provide dealers with this type of "mark-up" discretion increase the risk of pricing disparities among consumers based on race, national origin, and potentially other prohibited classes. To ensure compliance with fair lending regulations, the CFPB recommended that indirect lenders:

- Impose dealer markup controls or revise dealer markup policies;
- Monitor and address the effects of markup policies as part of a robust fair lending compliance program; and
- Eliminate dealer discretion to markup buy rates, while fairly compensating dealers using a different mechanism that does not result in discrimination, such as flat fees per transaction.[28]

The CFPB noted that it "will continue to closely review the operations of both depository and non-depository indirect auto lenders, utilizing all appropriate regulatory tools to assess whether supervisory, enforcement, or other actions may be necessary to ensure that the market for auto lending provides fair, equitable, and nondiscriminatory access to credit for consumers."[29]

We applaud the Consumer Protection Bureau and the Department of Justice for their vigilance and action on the abuses that dealer interest-rate markups cause. CRL believes that both agencies recent actions are a step in the right direction. Ultimately, the only way to effectively eliminate abuse is to end this practice.

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[28] *Id.* at 5.
[29] *Id.*

## VI. Conclusion

Community banks and credit unions play an important and essential role in this nation's financial market. There is a need for appropriate regulatory flexibility for small depositories. Congress and regulators must avoid any effort to use regulatory relief for community banks and credit unions as a vehicle for non deposit-taking lenders, mid-size and large financial institutions to avoid having the regulatory scrutiny and oversight that proved lacking in the build up to the financial crisis.

The need for regulatory flexibility must be balanced against the importance of consumer safeguards, an institution's safety and soundness, and the security of America's financial system as a whole. Federal financial regulators, like the CFPB, must be allowed to both protect the American people and ensure access to a broad, sustainable financial market.

I look forward to continuing to work with this Subcommittee, community banks and credit unions, non-depository lenders, their associations, and regulators, to ensure that all of these objectives are satisfied through law and responsible regulations. Thank you for the opportunity to testify today and I look forward to answering your questions.

## *Community Home Lenders Association*

## *Written Statement Submitted for the*

## *House Subcommittee on Financial Institutions and Consumer Credit Hearing [4/15/2015] -*

## *"Examining Regulatory Burdens on Non-Depository Financial Institutions"*

The Community Home Lenders Association (CHLA) is pleased to submit this written statement to the House Subcommittee on Financial Institutions and Consumer Credit, as it examines regulatory burdens imposed on non-depository institutions. CHLA writes in its capacity as the only national association exclusively representing non-bank mortgage lenders.

As the nation recovers from the housing crisis of 2008, not only have the indiscriminate lending practices that contributed to that crisis largely disappeared, but mortgage credit has tightened considerably, making it harder for credit-worthy families to buy a home. In this environment, many large banks have exited the home mortgage business or significantly curtailed their lending by imposing credit overlays that generally restrict loans to only the best credit quality borrowers.

Fortunately, non-bank lenders - many of them community based, smaller lenders - have stepped up their lending efforts, demonstrably improving access to mortgage credit for many of the borrowers the banks have left behind. For example, non-bank mortgage lenders now originate more than half of FHA mortgage loans, and securitize more than 50% of GNMA mortgage loan securitizations. For these reasons, it is critical that as Congress examines unnecessary regulatory burdens for mortgage lenders, that it not exclusively examine appropriate regulatory relief for banks and other depository institutions, but also consider non-bank mortgage lenders.

That is why the CHLA is pleased to work jointly with the Community Mortgage Lenders Association (CMLA) on a package of regulatory burden relief measures that would apply to smaller mortgage lenders, including non-bank lenders.. CHLA believes this package meets the ideal criteria for responsible regulatory relief - provisions which unnecessarily place a compliance or cost burden on smaller lenders, while not providing any substantive benefits to consumers. Moreover, relief under these provisions is only provided to smaller, responsible mortgage lenders. Following is a brief description of these provisions.

1. **Prioritize CFPB Examination Resources - by exempting Smaller Responsible Mortgage Lenders from Exams.** Since the CFPB does not have unlimited staff and resources, prudent supervision should entail prioritizing examinations where they do the most good for consumers. Non-bank lenders are already under the supervision of each state that they do business with, and subject to their examination and enforcement authority. Such lenders also do a substantial volume of business with FHA and the GSEs, which also impose a wide range of net worth and other supervisory requirements.

Therefore, for small non-bank lenders that are not the subject of a referral by another regulator, it is just common sense that the CFPB should not focus their limited examination resources on such lenders. Thus, an exemption should be provided from CFPB exams for responsible smaller lenders. Under language developed with CMLA, in order to qualify, a lender would have to be under an origination volume threshold and would have to originate over 95% of its mortgage loans as Qualified Mortgage (QM) loans - and would have to be "responsible" - ie., not be subject to a referral by another agency or subject to a cease and desist order.

**2. Prioritize CFPB Vendor Audit Resources - by exempting Smaller Responsible Mortgage Lenders from certain vendor oversight requirements.** Similarly, the CFPB engages in oversight of vendors utilized by mortgage lenders. Here too, this is simply a question of establishing an appropriate prioritization of CFPB resources in this area. An exemption from such oversight requirements is appropriate for this same category of responsible mortgage lenders. Under our proposal, eligible lenders must meet the same small lender, responsible conduct criteria cited above in the CFPB exam provision.

3. **Extend Small Servicer Exemptions to Include All Small Servicers.** By regulation, the CFPB has provided relief from certain servicing requirements to smaller banks and other depository institutions. To provide for more equitable treatment among all servicers, Congress should provide such exemptions to all small servicers, regardless of whether or not it is a bank or other depository institution.

In addition, small servicer exemptions should not be conditioned on the type of subservicers they retain to help service the loans. It is the volume of loans that are serviced that should determine a small servicer exemption, not whether a particular small servicer performs all servicing functions internally or whether it subcontracts out certain servicing functions, while maintaining responsibility for servicing the loan. Similar eligible criteria are used as the small lender exemptions cited above, except an additional servicer volume limit is also established, to ensure that this is limited to small servicers.

4. **Waive 3-day Waiting Period When Loan Terms Improve for the Consumer.** Current disclosure rules require that if there is a change in fees, costs or interest rate that cause the borrower's Annual Percentage Rate (APR) to change by more than a minimal amount, that a new

three day waiting period kicks in prior to being able to close on the loan. This is appropriate when loan terms change to the detriment to the consumer. But this new tolling requirement should be waived when the change results in a lower APR to the borrower. Insisting on a three day period in such case is just an inconvenience for the borrower, while providing no real protections, in this case, to a borrower whose loan terms have improved.

Together, these are reasonable, common sense regulatory relief provisions designed to promote the continued full participation of smaller, community-based non-bank mortgage lenders, and to avoid industry concentration, which is bad for consumers. We ask for consideration of these provisions.

# Statement of the Mortgage Bankers Association

## Subcommittee on Financial Institutions and Consumer Credit
## Committee on Financial Services
## U.S. House of Representatives

## "Examining Regulatory Burdens on Non-Depository Financial Institutions"

## April 15, 2015

1919 M STREET NW, 5th FLOOR • WASHINGTON, DC 20036 • MBA.ORG • (202) 557-2700

Chairman Neugebauer and Ranking Member Clay, thank you for the opportunity to submit a statement for the record of your hearing titled "Examining Regulatory Burdens on Non-Depository Financial Institutions."

The Mortgage Bankers Association (MBA)[1] uniquely represents mortgage lenders and servicers of all sizes and business models: from small independent mortgage bankers, community banks, and credit unions to the nation's largest financial institutions. MBA's members each play their own unique role in serving the mortgage financing needs of families across the country. In total, 700 of MBA's residential members – a total of 80 percent – are community lenders and approx 60 percent of these are IMBs.

Independent mortgage bankers, however, heavily dominate the origination of home-purchase mortgages. The independent mortgage banker share of that segment has increased from 25 percent in 2008 to 40 percent in 2013.These companies focus their lending on government-insured or guaranteed loans – Federal Housing Administration, Veterans Administration, and Rural Housing Services mortgages – that predominantly serve low-and moderate-income families and first-time homebuyers.

Independent mortgage bankers are typically "monoline" companies, focused exclusively on providing home mortgage financing, mortgage servicing and other closely related services. These companies can range in production volume from $100 million to more than $20 billion annually. They can have fewer than 100 employees or several thousand.

Independent mortgage bankers are well-regulated as both lenders and servicers, are subject to state supervision in every state that they do business, and also regulated at the federal level, where the Consumer Financial Protection Bureau (CFPB) has supervisory, investigative and enforcement authority over them – in addition to the numerous Dodd-Frank rules it has promulgated that cover them. In addition, Fannie Mae, Freddie Mac, Ginnie Mae and the Federal Housing Finance Agency have minimum net worth, capital and liquidity requirements for all approved lenders/servicers and routinely monitor their performance. Warehouse lenders, who provide financing to independent mortgage bankers, also closely monitor the companies – in the event the underlying collateral needs to be used due to defaults.

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mba.org.

Importantly, independent mortgage banks are the only lending model where each individual loan originator employed by the company is required to be licensed in each state in which they operate. This means the loan officer must take verified pre-licensing education courses, pass a licensing exam and maintain up-to-date continuing education requirements.

Since the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act, and the subsequent rulemakings the law required, the industry has been more focused on regulatory compliance than ever before. The new regulatory regime is also quite costly and many aspects of the Dodd-Frank rules are having a detrimental effect on the availability and affordability of mortgage credit for too many creditworthy families.

MBA data show that mortgage credit availability remains far below the levels seen prior to the mortgage crisis. Although credit has begun to loosen somewhat in recent months, particularly for jumbo borrowers, many borrowers continue to have difficulty qualifying for credit, or would pay much more for credit than was true before the crisis. No one would advocate going back to the weak credit standards that contributed to the boom and bust. However, the pendulum has swung too far, and credit standards could safely be changed – and pass-through costs due to regulatory burden reduced – to enable loans to additional qualified borrowers.

MBA has consistently supported reasonable requirements that will prevent a reemergence of any past excesses. While we believe the CFPB did commendable work in developing the Ability to Repay (ATR) rule including the Qualified Mortgage (QM) definition, we also believe the ATR rule and other aspects of Dodd-Frank warrant strong oversight and adjustment when they unnecessarily raise costs or limit access for creditworthy consumers. Such changes must be made judiciously to retain appropriate consumer protections while ensuring access to safe sustainable mortgage credit in a competitive market.

As explained here, we believe other changes to the Bureau's operations and requirements beyond the Bureau's purview also are warranted to facilitate the availability of credit.

**I. ATR and QM Background**

The ATR rule requires lenders to determine that a borrower has a reasonable ability to repay a mortgage before the loan is consummated. Dodd-Frank and this rule establish significant penalties and liability for failing to meet this requirement. The ATR rule provides a presumption of compliance with its requirements for loans that are originated as Qualified Mortgages, which provides greater certainty to lenders and mortgage investors regarding potential liability should a loan later default.

In order for a mortgage loan to qualify as a QM it cannot contain higher-risk features such as negative amortization or interest-only periods, and the sources of repayment must be fully documented. A QM must also meet specified underwriting standards

including that the borrower's debt-to-income (DTI) ratio must not exceed 43 percent or, in the alternative, the loan must be eligible for Fannie Mae and Freddie Mac (the GSEs) purchase or Federal Housing Administration (FHA) or other government programs. This alternative is commonly referred to as the "QM patch." In today's market the patch is essential since it offers and weighs a broader array of relevant underwriting factors than the alternative 43 DTI approach. However, the patch effectively hides the full impact of the QM rule by making all agency loans qualified mortgages.

Further, for loans to qualify as QM, borrowers also may not be charged points and fees that exceed three percent of the loan amount for loans in excess of $101,953 (in 2015). Loans below that amount are permitted to have fees in excess of three percent, based on a sliding scale; the lower the loan amount below the $101,953 threshold, the greater the points and fees permitted.

The rule establishes a compliance "safe harbor" for QMs if the Annual Percentage Rate (APR) of the loan does not exceed the average prime offer rate (APOR) for that mortgage by 150 basis points (bps) or more and the loan meets the other QM requirements. A safe harbor is a well-tested means of ensuring compliance with legal requirements. In that model, regulated entities are provided specific requirements and if they meet them, they are assured that any legal inquiry will be concerned only with whether the requirements were in fact met.

Loans to borrowers whose APRs exceed the APOR by more than 150 bps are not offered a safe harbor and instead receive a rebuttable presumption of compliance if their loans otherwise qualify as QMs. The level of additional risk under this standard versus the safe harbor has not yet been tested in litigation under Dodd-Frank.

Considering the significant potential liability and litigation expenses for an ATR violation, QM safe harbor loans currently comprise nearly all of the mortgage loans available in today's market. Few lenders are making either non-QM loans or rebuttable presumption QMs loans.

Moreover, the secondary market for non-QM loans remains extremely limited, and rate sheets from non-QM investors indicate a substantial risk premium exists for these loans. To date, affordable non-QM loans have generally been available only to higher wealth borrowers with broad financial relationships with institutions.

The CFPB recently proposed to amend its mortgage rules to facilitate lending by small and rural lenders by expanding the number of small creditors who receive QM status for loans held in their own portfolios when a consumer's DTI ratio exceeds 43 percent. Also, under the proposal an increased number of small creditors in rural or underserved areas would be able to originate QMs with balloon payments, even though loans with balloon payments are generally not permitted to qualify as QM loans.

## II. Recommended Changes to QM

### A. Framework for QM Changes

MBA believes it is time to consider changes in the QM definition to mitigate the adverse impact the initial rule has had on access to credit for some borrowers. We strongly believe these changes should be made holistically to the QM definition, and not limited to certain lenders based on charter types or business model. Consumers should not be forced to discern which institutions offer particular types of loans; their choices should not be limited to particular providers. Stratification of the market by establishing different underwriting standards for some lenders and not others only causes unnecessary consumer confusion and will lessen competition. A holistic approach to revising the QM will ensure a competitive market for all types of QM loans, and does not shift the burden to the consumer to figure out which lenders offer which QM products.

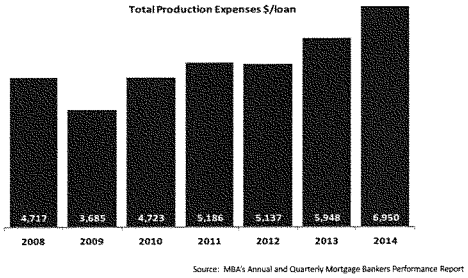
### B. Expand the QM Safe Harbor

Because of certain flaws in the definition of the Average Prime Offer Rate, the calculation is biased low as a measure of the typical prime mortgage in the market. In addition, the rate is pegged only weekly and therefore lags the market. In a volatile interest rate environment where interest rates can move up 50 basis points or more in few days, the 150 basis spread over the APOR may inadvertently knock many borrowers out of the QM safe harbor. MBA recommends that the spread over the APOR for defining a safe harbor QM be expanded to 200 basis points. This step alone would broaden the availability of credit by extending safe, sustainable QM loans to a greater number of creditworthy borrowers, particularly in a rising interest rate environment.

### C. Increase the Small Loan Definition

The current definition of a smaller loan under the ATR rule – where points and fees may exceed three percent and still qualify as a QM – is set at $101,953 for 2015. This definition is far too limited considering the costs of originating a loan.

Origination Production Costs – Also Up




Moreover, the average loan size today is approximately $260,000. Because of the current definition, too many smaller loans do not qualify as QMs. MBA recommends that the Bureau raise the definition to loans under $200,000, with a sliding scale that permits progressively higher points and fees caps for smaller loans. This change – which MBA would assert the Bureau has the authority to make by rule – would do much to serve the credit needs of low- and moderate-income borrowers who have smaller loan balances.

| **2015 QM Points and Fees Caps** | | **Recommended QM Points and Fees Caps** | |
|---|---|---|---|
| Loan Amount | Points and Fees Cap | Loan Amount | Points and Fees Cap |
| | | $200,000 and up | 3% |
| | | $150,000 to $199,999 | $6,000 |
| $101,953 and up | 3% | $100,000 to $149,000 | 4% |
| $61,172 to $101,952 | $3,059 | $80,000 to $99,999 | $4,000 |
| $20,391 to $61,171 | 5% | $20,391 to $79,999 | 5% |
| $12,744 to $20,390 | $1,020 | $12,744 to $20,390 | $1,020 |
| Less than $12,744 | 8% | Less than $12,744 | 8% |
| | | New tiers/caps | |

**D. Broaden Right to Cure for DTI and other technical errors**

MBA strongly advocated for an amendment to the QM rule to permit the cure or correction of errors where the three percent points and fees limit is inadvertently exceeded. We appreciate that the Bureau made this important amendment; such a change helped ameliorate any understandable conservatism that limits credit availability to borrowers. To encourage lending to the full extent of the QM credit box, MBA also urges that the right to cure or correct inadvertent errors be extended to DTI miscalculations and typographical and technical errors and omissions.

**E. Revise the "Points and Fees" Definition**

MBA strongly supported the passage of H.R. 685, the Mortgage Choice Act, which would exclude title insurance fees paid to lender-affiliated companies from the calculation of "points and fees" under QM. Currently, the ATR rule's points and fees calculation includes fees paid to lender-affiliated settlement service providers – but not to unaffiliated settlement service providers. Many MBA members use affiliated settlement service providers to deliver a more reliable consumer experience. This is particularly important as we transition to the new integrated TILA-RESPA disclosures where lenders are held accountable to meet narrow fee tolerances and tight disclosure timeframes. Furthermore, title insurance premiums are regulated in most states and the premium is the same whether or not the title company is an affiliate of the lender.

MBA believes that the rule should not discriminate against lenders that use affiliated settlement providers. Requiring that the affiliate's title premium be included in lender origination charges, but not those of non-affiliated title companies does a disservice to the consumer as well as lenders with affiliate providers. Such discrimination works to lessen choice and decrease competition for consumers. Most importantly, for many lenders it makes low balance loans serving low- and moderate-income borrowers much costlier to originate and consequently less available to consumers.

**F. QM for Portfolio Loans**

While we prefer a holistic fix for QM, certain aspects of the QM could be modified to recognize the alignment of lender-borrower interests in portfolio lending. MBA could support proposals for QM treatment of loans that do not meet the 43 percent DTI limit, and for certain balloon loans if they are held in portfolio for three years. The fact that a loan is to be held in portfolio can be an important check against originating unsustainable loans. However, we believe some of the other parameters of the QM should be retained for portfolio loans to protect against the re-emergence of loans with risky features such as pay option ARMs, stated-income underwriting, and short-term balloon terms.

Importantly, MBA also believes that the portfolio exemptions from the QM should be extended to originators that process, fund and sell these loans to a bank (or REIT) that

will retain the loans in portfolio for the required holding period. This could be particularly important for many community banks that are finding the costs and compliance burdens of maintaining a mortgage origination operation to be excessively burdensome, but wish to offer the portfolio products to their customers.

MBA believes that independent mortgage bankers who specialize and excel in mortgage origination should be permitted to originate portfolio QMs for sale to community banks. The community banks would maintain control over the credit and underwriting standards, and would retain the ability to enforce these standards through repurchase requirements should a loan not meet the required parameters. This approach expands the availability of portfolio QMs for community banks that cannot sustain the high costs of maintaining an origination platform in today's high compliance cost environment.

**G. Long-term Work on QM: Replace the Patch and the Default QM**

Unlike the 43 DTI test and the cumbersome guidelines set forth in Appendix Q, the QM patch provides compensating factors to better qualify consumers for affordable credit. While the QM patch is an essential feature of the ATR/QM rule at this time, it is intended to expire after seven years or when the GSEs leave conservatorship. Considering the importance of an alternative to the DTI formulation, MBA urges the CFPB to begin a process of working with stakeholders to develop a transparent set of criteria, including the use of compensating factors, to define a QM, replacing both the patch and the 43 percent DTI standard. Such a standard must provide workable, flexible underwriting standards that are consistent with Dodd-Frank but do not inject undue complexity or uncertainty into the process of serving consumers credit needs. A simpler approach would be to classify all loans for which the lender has determined the borrower's ability to repay as qualified mortgages.

**III. Other Impediments to Credit Access for Consumers**

In addition to changes to the ATR/QM rule, there are several other areas which we believe should be addressed to facilitate access to credit.

**A. Need for Authoritative Written Guidance Accompanying Rules**

Notwithstanding its preeminent role in consumer regulation, the Bureau has, with limited exceptions, followed a policy of only offering authoritative guidance in the form of formal rules and commentary. Most other guidance in the form of webinars, handbooks or other oral statements is prefaced with the caveat that only formal commentary and rules can be relied upon. While MBA believes that rules and commentary with an opportunity for public comment must remain the primary means of implementing the myriad laws for which the Bureau is responsible, the agency's reluctance to also offer authoritative written guidance – through FAQs or supervisory memoranda – as questions arise has made lenders excessively cautious and defensive in their approach to lending.

The final RESPA/TILA rule, comprising 1,888 pages, was issued on November 20, 2013, with an implementation date of August 1, 2015. The rule requires new, integrated disclosure forms to be provided to consumers at the time of mortgage application and settlement, known as the Loan Estimate and the Closing Disclosure, respectively. Most importantly, the rule brings major changes not just in the mortgage process, but also in the real estate transaction process. Under the new rule, both lenders and assignees face significant liability for failures to comply.

While the Bureau has produced several webinars and helpful issuances, and participated in a numerous conferences and forums, many questions regarding this uniquely detailed and complex rule have arisen and remain unanswered, and many more questions can be counted on before August 1. Notwithstanding, the Bureau has steadfastly refused to offer timely, accessible Frequently Asked Questions (FAQs) or other authoritative guidance to regulated entities as other regulators do, except for on a handful of technical amendments and commentary to address a small set of issues. The absence of timely, authoritative written guidance from CFPB has resulted in confusion and has complicated the implementation process. Most importantly, the lack of such guidance in some areas threatens to make borrower beneficial features of transactions such as lender credits toward closing costs far more difficult to sustain.

Considering the extensive liability that can arise from TILA violations, there is considerable concern that the new disclosures will open lenders to new liability. The CFPB has taken the position that the question of the nature of liability under the rule will be settled by the courts. In the meantime, however, such uncertainty can be expected to spawn litigation and ultimately increase costs for consumers.

Because of the lack of guidance on key issues and the need to review and amend parts of the rule, we have urged that the Bureau establish a reasonable grace period for enforcement and liability during the first six months of the rule's implementation. Such action would facilitate the provision of needed guidance, compliance in good faith and allow any impediments to implementation to be addressed.

**B. The Bureau Should Issue Guidance Prior to Enforcement**

Since the Bureau was established it has moved forcefully to enforce the laws it is charged with and publicly announced numerous and costly settlements. While MBA does not question the appropriateness of these efforts, we are concerned about an over-reliance on enforcement actions to drive industry compliance with the Bureau's new rules. Instead of issuing supervisory guidance, many of the Bureau's positions have been articulated through settlements rather than through guidance or rules. This approach – particularly regarding difficult and often subjective areas such as RESPA or unfair, deceptive, or abusive acts or practices (UDAAP) actions – opens up activities not previously believed prohibited to potential challenge by state regulators, plaintiffs' attorneys, as well as the government.

Most importantly, while both enforcement and clear rules of the road protect consumers, offering guidance upfront casts a wider net and protects borrowers against harm before it occurs by ensuring the compliance of the vast majority of lenders that want to comply. With no public rulemaking or supervisory guidance, even industry counsel becomes hesitant to provide lenders with reliable compliance advice. In this environment, fear of enforcement too frequently becomes the dominant driver of lender behavior, discouraging even meritorious interpretations of the rules to serve borrowers.

MBA supports Bureau or, if necessary, Congressional action to develop an appropriate framework for the issuance of rules, policies and supervisory guidance. This would include issuing Supervisory Memoranda or Compliance Bulletins to put industry on notice regarding supervisory expectations on specific problematic practices, along with suggested compliance practices. This is especially important in connection with CFPB's UDAAP authority. Such action will ensure that access to credit for consumers will not be harmed by unnecessary confusion or fear.

**C. Improvements Needed in CFPB Consumer Education Initiatives**

While MBA appreciates the Bureau's work to create several valuable education resources to improve consumers' choices, its recently posted "rate checker" tool and its recently announced policy to begin posting unverified consumer narratives to its complaint database threaten to mislead consumers, undermining the Bureau's other efforts.

*The Rate Checker*

In January of this year, the Bureau posted on its website a "rate checker" tool so borrowers could determine the interest rate for a mortgage loan in the state where the property is located. The tool was posted without any notice and opportunity to comment and notably does not include loan costs in its calculations.

Online rate checkers or trackers are inherently problematic because they tend to simplify markets and the collateral, borrower, and other factors that determine interest rates. The CFPB's rate checker is no different but raises even a greater risk of borrower confusion because it comes with the imprimatur of a government agency.

Although, the CFPB has made some minor revisions to the tool, significant problems remain, including:

- a flawed sampling methodology, which excludes independent mortgage bankers and community banks that today account for about 50 percent of the market for home purchases;
- a lack of specific data on discount points or origination fees associated with quoted rates;
- the failure to collect key data on the occupancy, property type (single family/condo), and use of proceeds (refi or purchase)

- the absence of an APR disclosure required in lender rate advertisements;
- exclusion of certain products such as the 20-year mortgage and the 5/5 ARM;
- lack of data collected about the borrower's income; and
- the absence of estimates made about a borrower's monthly principal and income payments.

*Complaint Database*

Similar problems are presented by the CFPB's recently announced decision to expand its consumer complaint database to include unsubstantiated consumer narratives to accompany complaints about lenders. Because the vast majority of consumer complaints lodged through the Bureau's complaints portal do not require remedial action, MBA urged in its comment on this change that CPFB narrow its postings to include only those narratives where the accuracy of the complaint has been verified. MBA also urged the Bureau to treat this undertaking as necessitating rulemaking so that the effects on small business and the economy were appropriately taken into account. The CFPB moved forward nonetheless and the final policy makes no provision for ensuring that complaint narratives are valid or accurate. Nor is there any process for removing complaints that are inaccurate or resolved with a simple explanation.

Like the "rate checker," rather than ensuring consumers are provided accurate information, the CFPB has chosen to put the Government's imprimatur on information that can mislead consumers and result in ill-informed choices. MBA has urged Bureau to reconsider these recent "consumer education" initiatives that are doing more to confuse than enlighten American consumers. With the rate checker and the posting of unsubstantiated narratives, the Government provides information that is incomplete, undermining borrowers' choices at a time when the mortgage industry has never been safer or more transparent.

**IV. Other Barriers to an Efficient Housing Finance Market**

**A. <u>SAFE Act Disparities</u>**

MBA has long supported the establishment of a sound qualification framework for all mortgage originators serving consumers, regardless of where they work. Unfortunately, while the Secure and Fair Enforcement for Mortgage Licensing (SAFE) Act seeks that objective, in its current form the Act does not provide consumers the necessary assurance that all Mortgage Loan Officers (MLOs) have met minimum standards of competency through an objective test.

The SAFE Act requires MLOs employed by non-bank lenders to be licensed, pass a comprehensive test, undergo criminal and financial background reviews, and register in the National Mortgage Licensing System and Registry. By contrast, under SAFE, MLOs employed by federally-insured depositories or their affiliates are registered in the NMLS but do not have to pass an objective test administered by a third party. Although most banks employ extensive training curriculums, a testing requirement would provide

consumers assurance that their LO meets minimum standards of competency and knowledge. In addition, the different standards under the SAFE Act make it difficult for MLOs to transition efficiently between employers of different charter types.

MBA urges Congress to amend the SAFE Act to require states to issue transitional licenses to individuals who are registered loan originators employed by a depository institution (or an affiliate). Similarly, a state-licensed loan originator in one state who takes a similar position in another state would have a transitional grace period to obtain a license in the new state. These individuals would be able to continue originating loans for a transitional period after being employed by a state-licensed non-depository entity willing to take responsibility for their activities during the transitional period.

In the long term, it is important to move toward a universal testing requirement that creates a level playing field for all MLOs. In the interim, this narrow and simple solution creating transitional licenses would allow all qualified individuals to satisfy borrowers' credit needs and maximize consumer choice while ensuring workforce mobility.

**B. FHFA Should Direct the GSEs to Use Updated Credit Scoring Models**

Another impediment to consumer access to credit is the use of outdated credit scoring models by the GSEs. The major consumer credit score model developers have announced changes to their credit scoring models with an eye toward making those models more accurate for today's borrowers in light of lifestyle changes and the post-recessionary risk environment. While the GSEs, in consultation with industry, have begun the process of analyzing and incorporating these new models, the continued required use of the outdated models harms today's borrowers. Among many factors, outdated credit scoring models may not accurately reflect the credit-worthiness of a borrower; for instance, medical debt and rent payment histories may not be given proper weight. The new models help to score borrowers with limited credit experience, i.e. "thin files."

MBA believes the Federal Housing Finance Agency (FHFA) should expedite the GSEs' validation and adoption of the latest validated credit scoring models.
Furthermore, the GSEs' delay in including the new scoring models into their automated underwriting systems may also cause lenders to hesitate to use them in their other lending products, as it could be viewed as an unfair practice to use different scoring models for different products.

**C. New Regulations Have Driven Up the Cost to Service Loans**

New servicing rules have dramatically driven up the cost to service loans and driven down efficiency in servicing operations. On the efficiency front, loans serviced per full-time equivalent employees have decreased from 1,638 in 2008 to 790 in 2014. Total cost to service loans has increased from $173 per loan in 2008 to $309 in 2014. Direct costs have increased from $55 per loan to $170 per loan during the same timeframe. Costs to service loans in default have risen from $423 per loan in 2008 to $2,214 in

2014. These additional costs ultimately get passed through to consumers on new loans. Likewise, these costs directly impact consumer access because defaulted loans cost so much more to service, and lenders reduce their exposure to lower FICO borrowers as a result.

**D. Basel III Limits Banks' Involvement in Mortgage Finance**

The U.S. bank regulators put in place the Basel III framework in recent years. Basel III reduces a bank's potential investment in mortgage servicing assets from 50 percent of Tier 1 capital to 10 percent of the common equity component of Tier 1 capital before they must be deducted directly from capital. Regulators also raised the risk-weighting of mortgage servicing rights from 100 percent to 250 percent. Thus banks that are close to these limits will be forced to sell the servicing on incremental mortgage production, making new mortgage production less attractive. That is why MBA would support bicameral efforts to move legislation that would mandate a study into the impact of Basel III on mortgage servicing assets owned by community banks and credit unions (a bipartisan bill, H.R. 1408 has already been introduced in the House). A moderation of Basel III's treatment of mortgage servicing assets would allow these smaller institutions to maintain responsible credit access for consumers, i.e., selling the loan asset to replenish lendable funds, while still maintaining the loan servicing relationship with the consumer.

**V. Conclusion**

We commend the efforts of the subcommittee to examine the regulatory hurdles facing non-depository financial institutions and the millions of consumers they serve. No matter how well-intentioned they may be, we are concerned that key federal rules and practices are unduly restricting credit opportunities for qualified borrowers.

We look forward to working closely with this subcommittee and with regulatory policymakers to improve the availability of sound mortgage credit for American families.

Prepared Testimony of

The National Association of Mortgage Brokers

on

"Examining Regulatory Burdens on Non-Depository Financial Institutions"

Before the

Committee of Financial Services

Subcommittee on Financial Institutions and Consumer Credit

Wednesday, April 15, 2015

The National Association of Mortgage Brokers appreciates this opportunity to address certain regulatory burdens that are having a significant adverse affect on consumers' ability to obtain mortgage credit.

NAMB is the only national trade association devoted to representing the mortgage broker industry. NAMB speaks on behalf of more than 50,000 mortgage professionals in all 50 states and the District of Columbia. Our members are independent, small business men and women who adhere to a strict code of ethics and best lending practices when assisting consumers through the loan process. We typically maintain business relationships with various lenders to provide consumers with multiple financing options. These partnerships allow our members to offer consumers the most competitive mortgage products available.

We commend the Committee for holding this important hearing to identify, examine and address the underlying burdens that non-financial institutions are facing today when seeking to provide mortgage credit.

## I. Summary

NAMB, like our sister trade groups, is very concerned that consumers are being harmed by certain unintended consequences stemming from regulatory requirements in the Dodd-Frank Act. Specifically, the steady rise in regulatory compliance costs, loan originating entities' fear of action by the Consumer Financial Protection Bureau, and a lack of clear and reliable regulatory guidance is adversely affecting the affordability and availability of mortgage credit for consumers and delaying our housing recovery.

The cost of regulatory compliance has surged beyond $7,000 per loan. As a result, mortgage broker companies, small lenders and community banks are increasingly leaving the primary mortgage origination market. With less competition, consumers across the board are facing increased costs. However, we are seeing a particularly disparate impact on low- and moderate-income borrowers.

NAMB believes this erosion of competition in the marketplace stems largely from a simple definitional error in the Dodd-Frank Act, which is greatly increasing the cost to consumers seeking loan amounts under $150,000 and making it virtually impossible for mortgage broker entities to serve those borrowers. Our testimony focuses on the harm this is causing consumers, the technical correction that we believe will solve this problem, and the impact of the non-depository broker business model.

## II. Dodd Frank Act - Creditor Payments to Broker Firms - Explanation of the Problem

NAMB believes that there is a definitional error in the Dodd-Frank Act affecting the calculation of points and fees for Qualified Mortgages. We are confident that it could not have been the intent of Congress to include payments from creditors to mortgage broker entities in the calculation of points and fees, because such payments are already included in the rate established and offered by the creditor. Nevertheless, under current CFPB regulations, mortgage broker companies are forced to double-count their business and operational costs within the 3% cap on points and fees for Qualified Mortgages while every other originating entity is not.

Mortgage broker companies are generally small businesses. With an increase in labor costs stemming from recent Department of Labor regulations, and with the steady increase in the cost of employee healthcare, small businesses are seeing their operational expenses skyrocket. The CFPB's interpretation of the Dodd-Frank Act as requiring only mortgage broker companies to double-count their business and operational expenses and still remain within the 3% cap for Qualified Mortgages places broker entities at a significant pricing disadvantage as compared with every other market participant.

Recently, the CFPB acknowledged this problem of double-counting in another area. In its final rule on Loan Originator Compensation issued May 29, 2013, the CFPB took corrective action

and excluded from the calculation of points and fees payments from mortgage broker companies to their employee loan officers.

> "Because payments by mortgage brokers to their employees already have been captured in the points and fees calculation, excluding such payments will facilitate compliance with the points and fees regulatory regime by eliminating the need for further investigation into the mortgage brokers' employee compensation practices, and by making sure that all creditors apply the provision consistently. [Emphasis added] It will also effectuate the purposes of TILA by preventing the points and fees calculation from being artificially inflated, thereby helping to keep mortgage loans available and affordable by ensuring that they are subject to the appropriate regulatory framework with respect to qualified mortgages and the high-cost mortgage threshold." CFPB Final Loan originator compensation rule, page 76 May 29, 2013.

This was extremely helpful, and we believe a correct interpretation of the Dodd-Frank Act. However, despite identifying the same problem of double-counting with creditor payments to mortgage broker companies, and despite acknowledging that mortgage broker companies are at a disadvantage vis-a-vis their competitors, the CFPB remains unable, in their estimation, to take similarly necessary corrective action with regard to creditor payments to mortgage broker companies. The reason for this, cited by the CFPB, is because of language in the Dodd-Frank Act attempting to define which mortgage entities' fees should be included in the points and fee calculation for purposes of determining a Qualified Mortgage. In relevant part, Section 1431(c)(A) of the Dodd-Frank Act (current Section 103(bb)(4)(B) of TILA) provides:

> "(B) all compensation paid directly or indirectly by a consumer or creditor to a mortgage originator from any source, including a mortgage originator that is also the creditor in a table-funded transaction;"

Experts within and outside of the CFPB believe this definitional language, which is preventing the CFPB from excluding creditor payments to mortgage broker companies from the calculation of points and fees, is actually a drafting error in the Dodd-Frank Act.

Any amount that is already reflected in the rate of a loan should not be included in the calculation of points and fees. The CFPB utilized it's Congressionally-granted power to exclude from the Qualified Mortgage definition of points and fees any payments from a creditor to the creditor's employees. In its release published in the Federal Register June 12, 2013, (78 FR 35429), the CFPB additionally pointed-out that a similar result should occur for payments from lenders to mortgage broker companies and their loan originator employees since such fees are already reflected in the mortgage rate and are being counted twice.

> "The final rule excludes from points and fees loan originator compensation paid by a consumer to a mortgage broker when that payment has already been counted toward the points and fees thresholds as part of the finance charge under § 1026.32(b)(1)(i). The

> final rule also excludes from points and fees compensation paid by a mortgage broker to an employee of the mortgage broker because that compensation is already included in points and fees as loan originator compensation paid by the consumer or the creditor to the mortgage broker."

This principle is further supported and extended by the CFPB in it's Final Rule on Integrated Mortgage Disclosures that takes affect on August 1, 2015. In that final rule the CFPB declared that the disclosure of mortgage broker compensation is not a beneficial aspect of the transaction and only confuses the consumer as to the consumer's real costs for the transaction. As such, beginning August 1, 2015 mortgage brokers will no longer be required to disclose on the Loan Estimate and Closing Disclosure Forms any compensation they receive from the creditor.

The option for a consumer to select a market rate above par alleviates the need for the consumer to pay a mortgage broker company any fee out of consumer's personal funds. The above par rate enables the creditor to compensate the mortgage broker company directly. This being the case, a payment from a creditor to a mortgage broker company should not be counted in the 3% cap on points and fees for Qualified Mortgages because this payment is already accounted for within the interest rate chosen by the consumer.

In order for a fair and competitive marketplace to be reestablished, payments from a creditor to a mortgage broker company must be excluded from the Qualified Mortgage points and fees calculation.

## III. Lack of Competition Hurts Consumers

Empirical studies have shown that mortgage brokers offer better terms, on average, than depository lenders and other creditors.[1] Specifically, these studies show that in areas with a higher concentration of mortgage brokers consumer choice is greater and consumers generally receive lower interest rates from brokers in that area.[2] Conversely, where there are fewer mortgage brokers competing in a given market and thus less competition, consumers typically pay higher interest rates.[3]

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[1] Amany El Anshasy, Gregory Elliehausen & Yoshiaki Shimazaki, *The Pricing of Subprime Mortgages by Mortgage Brokers and Lenders* 12 (July 2005) (unpublished manuscript), *available at* http://www.chicagofed.org/digital_assets/others/events/2005/promises_and_ pitfalls/paper_pricing.pdf (finding that "broker-originated mortgages are less costly to the borrower than lender-originated mortgages after holding other loan terms and borrower characteristics constant")

[2] *See* M. Cary Collins & Keith D. Harvey, *Mortgage Brokers and Mortgage Rate Spreads: Their Pricing Influence Depends on Neighborhood Type*, 19 J. HOUSING RES. 153, 168 (2010) ("Our results support our hypothesis that the mortgage broker is a better informed agent and show that in general as mortgage broker density increases, both the likelihood of a rate spread occurring and the size of a rate spread declines, while the loan approval rate increases."

[3] See id at 167–68.

As an example of this, a recent examination of closed loans in Duval County Florida found that the average net consumer closing costs for a creditor transaction was $6,222, while the net cost to consumers in broker transactions, after credits were applied, was $3,479. This is a greater than $3000 per loan cost savings for consumers obtaining loans from mortgage brokers. We believe that further examination and analysis of this pricing disparity between creditor and mortgage broker transactions will reveal similar results across the country.

NAMB is deeply concerned that without a correction to the definitional error in the Dodd-Frank Act there will be fewer and fewer mortgage broker companies in many areas, and a significant disparate impact will be felt by low- and moderate-income consumers who have no option but to obtain loans from large national banks. This is an unfortunate reality that is already affecting many consumers across the country and should not be allowed to get any worse. We respectfully urge this Subcommittee and Congress to take corrective action as soon as possible.

## IV. Mortgage Company Fixed Compensation

Since 2011, all compensation paid by creditors to mortgage broker companies is fixed, without any possibility for variation from transaction to transaction, as a result of the Loan Originator Compensation Rules issued by the Federal Reserve Board and the CFPB. This is a strong additional layer of consumer protection for borrowers utilizing a mortgage broker company and another reason why creditor compensation to a broker company should not be double-counted in the definition of points and fees.

Under these parameters, not only are loan originators working for mortgage broker companies prohibited from steering consumers toward a particular loan or lender, there is no incentive for them to do so. Making the small, but significant correction to the definition of points and fees in the Dodd-Frank Act that NAMB is encouraging will not put consumers at any risk. Rather, this simple change in definition will work to protect consumers from harm by preserving and enhancing competition, and saving consumers money at the closing table.

## V. Policy Recommendations Conclusion

NAMB thanks the Subcommittee for this opportunity to submit testimony for the record. We believe compensation paid from the creditor to a mortgage broker company, which is taken into account when the creditor sets the interest rate, should not be included in the 3% points and fees calculation for Qualified Mortgages. We look forward working with the Subcommittee to correct what we believe is merely a definitional error and resolve this unintended consequence of the Dodd-Frank Act in order to alleviate any further harm to consumers and help preserve and restore competition to the marketplace.

**Statement of the African American Credit Union Coalition**

Lynette Smith
Board Chairman

Mark S. Brantley, Esq.
Vice-Chairman and Advocacy Chair

**House Committee On Financial Services**
**Subcommittee on Financial Institutions and Consumer Credit**

Hearing on
"Examining Regulatory Burdens on Non-Depository Financial Institutions"

April 15, 2015

Chairman Jeb Hensarling, Ranking Member Maxine Waters, and members of the Committee, the African American Credit Union Coalition (AACUC) is pleased to submit this statement in connection with the House Committee on Financial Services' Subcommittee on Financial Institutions and Consumer Credit hearing on "Examining Regulatory Burdens on Non-Depository Financial Institutions" scheduled for April 15, 2015. The AACUC is a national organization of African-American credit union professionals and volunteers created to strengthen the global credit union community through diversity, professional development, and advocacy.

Established in 1999, the organization has individual members across the country and member organizations that include credit unions, vendors, and

associations. AACUC members serve at credit unions both large and small and from various regions. Through their respective institutions, our diverse membership provides financial services to urban communities as well as those in rural and suburban areas. AACUC's membership also reaches across the Atlantic into the Caribbean and Africa. Just recently, we sponsored the training of two credit union development educators (CUDEs) in South Africa who will play an integral part in the exchange of ideas and resources with credit union leaders in that country. According to the Credit Union National Foundation, CUDEs "provide critical lessons in cooperative principles, credit union philosophy and international development issues while incorporating challenges credit unions face today." The AACUC proudly continues to be the premier African American trade organization in the credit union industry.

**I. Credit Unions**

Credit Unions are not-for-profit, member-owned cooperatives with over one hundred million members and one trillion dollars in assets collectively. Our membership strength and growing balance sheet are indicative that the American people trust credit unions as a safe harbor for their financial wellbeing. For decades, credit unions have promoted thrift and delivered quality, affordable products to its members. The industry motto, "not for profit, not for charity, but for service" resonates through every financial transaction. Service is the primary motive, and when profits are realized, they are returned to members via lower interest rates and/or nominal fees. Credit unions have established a special niche in the financial services industry as "Main Street's" preferred depository institution.

Since the first financial services cooperative was established in 1909, hard-working Americans have relied on credit unions for access to credit. Credit unions have always been the affordable, safe alternative to traditional depository institutions and the antithesis to non-traditional, non-depository entities. On the financial frontline, credit unions continue the fight against redlining, predatory lending, loansharking, and other deceptive loan and credit practices.

During the financial crisis, credit unions received no bailouts. While other financial institutions were extended taxpayer assistance, credit unions paid into their own insurance share and stabilization funds to support the balance sheets of the corporate credit unions that suffered huge losses. After the crisis, loans for homes, automobiles, debt consolidations, and small businesses were provided by credit unions when other financial services companies restricted credit and kept cash in their coffers. Credit unions will always be there for those looking for their first home, first car, or sending their first child to college. In times of bust or boom, under-regulation or over-regulation, Americans continue to make credit unions their first choice in their pursuit to access credit.

**II. Pay Day Lending**

Millions of Americans are trapped in the endless debt cycle of payday lending. Despite the astronomical rates of interest and penalizing fees, payday lending remains attractive to consumers because of providers' high-speed delivery channels. Unlike depository financial institutions, pay day lenders have little to no underwriting requirements. These subprime small-dollar loans are processed at a substantially faster rate than credit unions or other depository institutions that are

required to review credit reports, employment history, etc. Requiring payday lenders to undergo similar underwriting processes as credit unions and/or other depository institutions would help protect consumers from unscrupulous and predatory lenders. Consequently, loan products delivered by non-depository financial institutions at the same approval rate of speed as traditional institutions would effectively eliminate the "quick fix", debt cycle solution that consumers find attractive.

As cooperatives, credit unions are uniquely positioned to offer responsible financial services to members. A credit union is cooperatively owned, democratically controlled and directly governed by its membership. This governance structure imputes a fiduciary duty on the credit union for the benefits of the membership. One could distinguish this legal perspective with that of payday lenders who owe no fiduciary duty to consumers. Consequently, customers engage in adversarial transactions with payday lenders. Requiring payday lenders to affirmatively ascertain a suitability standard for borrowers helps ensures consumers are treated fairly.

Fortunately, through the leadership of the National Credit Union Administration (NCUA), a payday alternative program framework was established. Credit unions now offer its members affordable, low cost small dollar loans. Since credit unions are not-for-profit depository institutions, where service is the priority over profits, these loans are offered in the spirit of the credit union philosophy of "people helping people." That is the credit union way!

For example, in June 2014, the $2 billion asset-sized Municipal Credit Union of New York (MCU) announced its "Step Line of Credit" payday alternative loan program at the Clinton Global Initiative in Denver, Colorado. This no fee, no late penalty, modest fixed rate loan product not only assists members with access to emergency funds for pressing financial needs, but it also doubles as a credit builder. Members however, are required to call the institution's hotline to speak to a "triage" specialist who will offer complimentary credit counseling services in conjunction with the loan. This holistic approach addresses the underlying economic as well as behavioral issues of the borrower. Similarly, small dollar loan programs are offered in the state of Georgia, where the "Phoenix" loan was established at the Credit Union of Atlanta. There, alternative payday loans are provided to assist members with small, unplanned expenses despite not having the best FICO score.

Therefore, we ask that the Committee and the Consumer Protection Financial Bureau (CFPB) in its efforts to curtail payday lending, please be mindful of the safe, affordable and responsible alternatives credit unions are providing its members.

**III. Qualified Mortgages**

According to the CFPB, a "Qualified Mortgage (QM) is a category of loans that have certain, more stable features that help make it more likely that you'll be able to afford your loan. Moreover, a lender must make a good-faith effort to determine that you have the ability to repay your mortgage before you take it out." While we certainly agree with CFPB's premise that every lender should make a good faith effort to determine ability to repay, creating criteria too strictly to determine affordability may impact some credit union members.

Credit unions have been responsible lending institutions for decades and have maintained the best underwriting practices in the financial services industry. Prior to the QM rule, credit unions were not engaged in predatory mortgage lending and neither did credit unions contribute to the financial crisis when the housing bubble burst. Credit unions uniquely offered a personal hands-on strategy and not a cookie-cutter approach in the underwriting of mortgages. They provide responsible borrowers that may not fit into a particular box, the opportunity at homeownership some applicants would not otherwise receive. With this in mind, credit unions will do their best to maintain this approach in assisting borrowers on the creditworthy fringes with the hope their lending practices will not fall outside the QM framework.

The AACUC and the entire credit union movement share the goals of the Committee and the CFPB to ensure consumers obtain safe and affordable mortgages. Credit unions have been providing mortgages to credit-worthy borrowers that fall both in and outside the margins of QM, and to the extent possible they will continue to do so. We look forward to working with the Committee and the CFPB to ensure as many creditworthy borrowers as possible are able to realize the American dream of homeownership.

**Conclusion:**

Credit unions have provided valuable and needed financial services to all communities including those of color. Since the early 1900's, the industry has been a stalwart in providing access to credit. Credit unions grant loans that other

institutions do not want to make. Hard working Americans trust and depend on credit unions as their financial partner.

The AACUC would like to thank you for the opportunity to share this written statement as part of the hearing record.

**Consumer Federation of America**

**Written Testimony of Consumer Federation of America**
**Submitted to the**
**Subcommittee on Financial Institutions and Consumer Credit**
**U.S. House of Representatives**
**Washington, D.C.**

**April 15, 2015**

Consumer Federation of America (CFA)[1] is pleased to submit written testimony to the Subcommittee on Financial Institutions and Consumer Credit, Committee on Financial Services as part of the Subcommittee's consideration of current and pending regulations that impact non-depository financial institutions. The harmful practices of payday and auto title lenders, and the importance of effective regulations to protect consumers from abusive practices is of particular concern. The comments provided below address two pending regulatory actions: the working draft of possible payday, auto title and payday installment rule released by the Consumer Financial Protection Bureau (CFPB); and the proposed rule to improve the Military Lending Act under consideration by the Department of Defense (DoD).

## 1. A Strong CFPB Rule is Necessary to Protect Consumers from the Financial Harm Caused by Payday, Auto Title and Payday Installment Loans

Currently 35 states authorize triple digit interest rate payday loans made without any consideration of a borrower's ability to repay.[2] As a result 71 percent of Americans live in states that would see a considerable improvement in consumer protections for payday and auto title loans if a strong CFPB rule is enacted. According to the Center for Responsible Lending, the failure to limit repeat, abusive borrowing results in $3.5 billion in additional fees paid by payday loan borrowers[3] and $3.6 billion in additional fees paid by title loan borrowers each year.[4]

As a data-driven regulator committed to improving the financial market place and protecting consumers, the CFPB has exhaustively documented the frequency of repeat borrowing and other harmful practices that its current proposal seeks to address. In March 2014, the CFPB released research documenting that repeat borrowing is standard practice—over 80 percent of loans are renewed because a borrower is unable

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[1] CFA is an association of over 250 nonprofit consumer organizations that was established in 1968 to advance the consumer interest through research, advocacy and education.

[2] *State Payday Loan Regulation and Usage Rates*. The Pew Charitable Trusts, July 11, 2012. http://www.pewtrusts.org/en/multimedia/data-visualizations/2014/~/media/Data%20Visualizations/Interactives/2014/State%20Payday%20Loan%20Regulation%20and%20Usage%20Rates/Report/State_Payday_Loan_Regulation_and_Usage_Rates.pdf.

[3] Parrish, Leslie, and Uriah King. *Phantom Demand: Short-Term Due Date Generates Need for Repeat Payday Loans, Accounting for 76% of Total Volume*. Washington, DC, July 9, 2009. http://www.responsiblelending.org/payday-lending/research-analysis/phantom-demand-final.pdf.

[4] *Driven to Disaster: Car-Title Lending and Its Impact on Consumers*. Washington, DC: Center for Responsible Lending and Consumer Federation of America, February 28, 2013. http://www.responsiblelending.org/other-consumer-loans/car-title-loans/research-analysis/CRL-Car-Title-Report-FINAL.pdf.

to repay in full and on time and half of all loans are part of a series of ten or more loans.[5] In a 2013 white paper on payday lending, the CFPB also found that 75 percent of loan fees were charged to borrowers that used 11 or more payday loan in a 12 month period.[6]

***The ability to repay standard proposed by the CFPB will protect consumers***

At a March 2015 field hearing in Richmond, Virginia, the CFPB issued a working draft of possible consumer protections under consideration for a proposal rule – a critical first step to ensuring that consumers are protected from abusive practices such as poor underwriting and back-to-back lending. The proposal contains a straight-forward, common-sense ability to repay standard that requires lenders to review borrowers' income and expenses before issuing a loan to ensure that they can repay the loan in full and on time without additional borrowing. The adoption of such a standard that applies to short-term and long-term payday and auto title loans, without loopholes for unsafe repeat borrowing, is critical to protecting consumers and stopping the debt trap caused by unsafe credit products.

***Preventing loopholes in a final rule is critical to a successful rule that protects consumers and a competitive market***

The CFPB proposal rightly applies the ability to repay standard to short- and long-term payday and auto title lending, as well as to similar, harmful products structured as open-end lines of credit. The broad scope of the proposal is fundamental to protecting consumers and to ensuring that lenders do not develop new products to evade a final rule. Likewise, the broad scope of the proposal also seeks to ensure that lenders seeking to comply with important consumer protections enjoy fair competition.

A 2014 report by payday lending analysts Stephens, Inc., illustrates the need to apply consumer protections to both short- and long-term payday and auto title loans and open-end credit by highlighting the shift from balloon payment payday loans to payday installment loans among storefront lenders. The Stephens report found that, as of 2014, installment loan growth represented well over half of the total growth for payday industry participants who experienced growth in 2013."[7] One of the largest lenders, Cash America has also shifted from balloon payment payday loans to longer-term payday loans and open-end lines of credit. Including both storefront and online lending, Stephens, Inc. noted that Cash America's installment and open-end products now comprise about 56 percent of the company's domestic loan balance as of December 2013.[8]

The broad scope of the proposal will ensure that lenders do not exploit common loopholes in state laws that are intended to protect consumers from short-term payday and auto title loans, but leave them susceptible to triple digit interest rates and poorly underwritten longer-term loans. However, the CFPB is also proposing a series of exemptions from the ability to repay standard that undermine its effectiveness.

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[5] *CFPB Data Point: Payday Lending*. Washington, D.C.: Consumer Financial Protection Bureau, March 2014. http://files.consumerfinance.gov/f/201403_cfpb_report_payday-lending.pdf.

[6] *Payday Loans and Deposit Advance Products: A White Paper of Initial Data Findings*. Washington, DC: Consumer Financial Protection Bureau, April 13, 2013. http://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf.

[7] Hecht, John. "Alternative Financial Services: Innovating to Meet Customer Needs in an Evolving Regulatory Framework." presented at the CFSA Solutions, Little Rock, AR, February 27, 2014. http://cfsaa.com/Portals/0/cfsa2014_conference/Presentations/CFSA2014_THURSDAY_GeneralSession_JohnHecht_Stephens.pdf.

[8] Ibid. Note that Cash America has since spun off its online lending operation, Enova Financial.

Of particular concern, the proposal allows lenders to make up to three back-to-back payday loans without a review of the borrower's income and expenses. This exemption could harm consumers if adopted in a final rule since it would, in effect, serve as a stamp of approval for back-to-back lending and could undermine stronger state protections, particularly those states that limit interest rates through state usury laws. CFA has urged the Bureau to issue a rule that does not include exemptions to the ability to repay standard and that combines both prevention and protection measures.

***Borrowers can and do turn to lower-cost, more sustainable financial options if abusive, back-to-back lending is restricted***

A strong rule would not unduly reduce access to safe and sustainable credit options. Instead it would ensure that all lenders, including storefront and online lenders, are only issuing loans that a borrower can repay without entering into a long-term cycle of debt.

In 2012, the Pew Charitable Trusts issued a report examining how borrowers would manage their financial options if high-cost payday lending was unavailable. The report found that 81 percent of borrowers that used payday loans would cut back on expenses. Borrowers also indicated that they would borrow from family or friends or sell or pawn possessions instead of taking out a high-cost payday loan. Likewise, 44 percent indicated that they would take a loan from a bank or credit union, 37 percent would use a credit card and 17 percent would borrow from an employer.[9]

A strong rule based on an ability to repay standard that applies to the entire payday and auto title market would serve the dual purpose of preventing widespread, well-documented abuses and giving borrowers the option of turning to lower-cost and more sustainable credit options as they already do in states that do not allow payday and auto title lending. While the proposal as currently structured may ultimately limit the number of back-to-back loans, this should be viewed as a dramatic improvement in a marketplace where over 80 percent of all loans are followed by another loan just days or weeks later.

**2. Additional Regulations are Needed to Protect Service Members from Financial Abuse**

The Department of Defense is currently considering modifying the rule implementing the Military Lending Act. The proposed rule, if adopted, would protect Service members from the loss of security clearance, involuntary force separation and financial insecurity as a result of using high-cost payday, auto title and other loans made with no consideration of the Service members' ability to repay. The proposed rule closes a number of well-documented loopholes created by the initial rules implementing the Military Lending Act and is supported by over 180 consumer, community and civil rights groups,[10] 22 state Attorneys General,[11] members of The Military Coalition[12] and others.

The Department of Defense recognizes the harm caused by payday, auto title and other high-cost loans and has previously stated that "predatory lending undermines military readiness, harms the morale of

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[9] *Payday Lending in America: Who Borrows, Where They Borrow, and Why*. Washington, DC: The Pew Charitable Trusts, July 2012. http://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2012/PewPaydayLendingReportpdf.pdf.

[10] Comment letter submitted to the Department of Defense available at http://www.consumerfed.org/pdfs/1412122_DoD_RIN-0790-AJ10_nationalandstate_letter.pdf

[11] Comment letter submitted to the Department of Defense available at http://1.usa.gov/1IXQvWO

[12] Comment letter submitted to the Department of Defense available at http://1.usa.gov/1FGxOJF

troops and their families, and adds to the cost of fielding an all-volunteer fighting force."[13] In 2013, the Department of Defense also described payday lending as "the biggest, current financial challenge facing our Service members, Veterans, and their families."[14]

***Loopholes in the current rule implementing the Military Lending Act put Service members' financial security at risk***

In 2006, Congress passed the Military Lending Act (MLA) as part of the John Warner National Defense Authorization Act of 2007. The MLA was enacted to protect active-duty Service members and their dependents from high-cost loans and other predatory credit practices that adversely impacted their military readiness. The MLA caps total interest and fees at 36 percent and bans harmful credit product features such as: renewals and refinances that do not benefit the borrower; forced arbitration; prepayment penalties; use of checks, vehicle titles or other automatic methods of access to the borrower's bank account; and requiring repayment by allotment as a condition of the extension of credit.

As part of the Military Lending Act, Congress authorized the DoD to define the scope of consumer credit and creditors covered by the MLA. The DoD subsequently issued its rule defining "consumer credit" that took effect on October 1, 2007 and applied the Act's protections only to closed-end payday loans of $2,000 or less with a loan term of 91 days or less, closed-end vehicle title loans with a loan term of 181 days or less, and tax refund anticipation loans. These narrow definitions were easily evaded by lenders who modified products to fall outside the rule's scope by either lengthening the loan term or structuring the loan as an open-end line of credit. For example:

- ***400 percent Title Installment Loan*** - A South Carolina lender made a vehicle title loan to a Service member on June 24, 2011 on a 13 year old car. The loan amount was $1,615 to be repaid in 32 months with $15,613 in interest at a 400 percent annual percentage rate. The title loan was exempt from the current rule's scope as the loan term exceeded 181 days. The loan included a forced arbitration clause that would have been prohibited if the loan was covered by the MLA.

- ***584 percent Open-end Line of Credit*** - Prior to the enactment of the MLA, one military lender made traditional closed-end payday loans but then changed its product to open-end payday loans that are exempt from the current rule's scope. A 2012 monthly activity statement discloses a "584.68 Annual Percentage Rate" on a loan balance of $2,000, plus other fees.

- ***360 percent Online Installment Loan*** - A sailor borrowed $500 from an online lender in 2012 and was charged $523 in interest for a total repayment of $1,024 for a loan over 140 days. Since the term of the loan exceeded 91 days the MLA protections did not apply.

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[13] *Report On Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents*. Washington, DC: Department of Defense, August 9, 2006. http://www.defense.gov/pubs/pdfs/report_to_congress_final.pdf.

[14] Testimony of Colonel Paul Kantwill, Director of Legal Policy, Office of the Undersecretary for Personnel and Readiness, Department of Defense before the Senate Committee on Veterans Affairs on July 31, 2013 available at http://www.veterans.senate.gov/imo/media/doc/kantwill-7-31-13.pdf

***DoD has documented the harmful effects of payday, auto title and other products on Service Members***

Recognizing that loopholes in the 2007 rules have allowed lenders to evade the MLA protections, Congress required DoD to issue a report to evaluate the impact of abusive credit on Service members' financial readiness. In April 2014, DoD issued their report, "Enhancement of Protections on Consumer Credit for Members of the Armed Forces and Their Dependents." The report included the results of a Service member survey and feedback from military financial counselors and found that 11 percent of enlisted Service members continue to turn to high-cost credit options. The report found that military financial counselors overwhelmingly reported that Service members would not be negatively impacted if access to high-cost credit was restricted. The findings suggested that applying the 36 percent rate cap on a product-by-product basis is unlikely to reduce the accessibility of high-cost and abusive credit. DoD concluded that an expanded and comprehensive definition of consumer credit would be a more effective approach to protect Service members from high-cost, abusive credit.

***The proposed rule protects Service members by applying military financial protections to the entire high-cost credit market***

The proposed rule closes the loopholes in the current rule by expanding the definition of consumer credit under the Military Lending Act to include products that are currently subject to the protections of TILA. Rather than taking a product-by-product approach, the proposed rule will prevent lenders from exploiting Service members by ensuring that high-cost products with abusive terms are covered by the protections established by the MLA regardless of the term of the loan or the loan's structure.

For example, the proposed definition of covered consumer credit would prevent lenders from structuring payday loans for longer than 91 days or larger than $2,000 for the purposes of charging higher rates. It would also stop lenders from structuring auto title loans as longer than 181 days or issuing high-cost, open-end lines of credit with abusive features that are currently exempt. Likewise, the proposed rule would cover additional high-cost products that negatively affect a Service members' financial security, such as high-cost overdraft lines of credit and abusive installment lending.

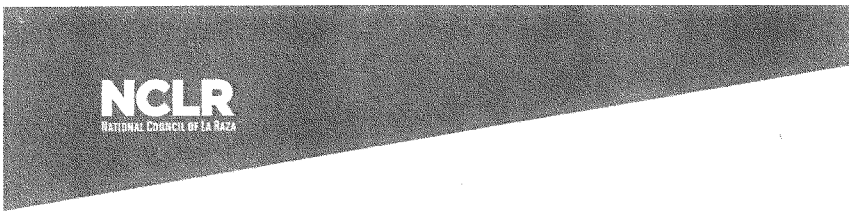
The proposed rule also addresses widespread concern about the use of add-on products. It ensures that certain additional charges, such as single premium credit insurance, debt cancellation, debt suspension or other ancillary fees are included in the calculation of interest and are capped as part of the MLA's 36 percent interest and fee cap. Add-on products, such as insurance products, often serve as a way to increase revenue in states that restrict interest rates and significantly increase the total cost of borrowing beyond the disclosed annual interest rate.

While the proposed rule would also apply the MLA protections to credit cards for the purpose of preventing abusive lenders from using high-cost credit cards to avoid MLA protections, DoD provided important exemptions for bona fide, reasonable and customary credit card fees. Most credit cards in the marketplace would be excluded from the rule, and Service members that rely on these products to meet their credit needs would not be affected.

The proposed rule strikes an appropriate balance between access to credit and restricting access to high-cost abusive credit. The proposed rule provides a targeted restriction for credit products that have been shown to negatively impact Service members' financial security, and ensures access to lower-cost options such as the $142 million in no-cost loans provided by Military Relief Societies in 2012.

### 3. Conclusion

Effective regulation of the lenders that offer high-cost payday, auto title and other loans is critical to protecting consumers and Service members from abusive practices and the financial insecurity that results from the sustained use of high-cost debt. The rules under consideration by the CFPB and DoD are the result of a comprehensive analysis of the high-cost credit marketplace and are the result of considerable research. They represent targeted responses that prevent bad practices so that good practices can flourish. We urge members of the subcommittee to carefully weigh the cost of compliance for lenders with the profound harm suffered by consumers and Service members that turn to high-cost credit to meet a short-term need only to learn that they often spiral into a long term problem.




# Protecting Latinos and Low-and Moderate- Income Consumers from Predatory Lending

Presented at

"Examining Regulatory Burdens on Non-Depository Financial Institutions"

Submitted to
Subcommittee on Financial Institutions and Consumer Credit

Submitted by
National Council of La Raza

April 15, 2015

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The National Council of La Raza (NCLR)—the largest national Hispanic civil rights and advocacy organization in the United States—works to improve opportunities for Hispanic Americans. Through its network of nearly 300 affiliated community-based organizations, NCLR reaches millions of Hispanics each year in 41 states, Puerto Rico, and the District of Columbia. To achieve its mission, NCLR conducts applied research, policy analysis, and advocacy, providing a Latino perspective in five key areas—assets/investments, civil rights/immigration, education, employment and economic status, and health. In addition, it provides capacity-building assistance to its Affiliates who work at the state and local level to advance opportunities for individuals and families.

NCLR's Office of Research, Advocacy, and Legislation (ORAL) is one of the most influential and visible national advocacy voices championing public policy on behalf of Latinos. In order to achieve its mission, ORAL is composed of several departments and issue-focused policy projects that: 1) gather and share information, research, and data on Latinos; 2) develop policy analyses, proposals, and ideas; 3) equip Hispanic-serving community leaders and NCLR Affiliates with information that empowers and engages them in public policy debates; and 4) provide decision-makers with strategic advice on how best to advance policy issues for Latinos.

Latino families share the same fundamental goals of financial security and upward mobility as the majority of Americans. To achieve the security that has long characterized the middle class, most rely on financial tools, including homeownership, to gradually expand their access to wealth-sustaining or income-generating assets. Building positive net-worth and an asset-based financial safety net often takes years or even decades. A true transformation of the Latino community will come when assets are successfully maintained over their lifecycle and passed to their children. Unfortunately, attainment of this goal has been impeded for a significant number of Hispanic families. Current economic conditions have exacerbated the historical and systemic barriers that Hispanic households confront when connecting with entry-level financial tools and long-term assets.

In the wake of the near collapse of financial markets in 2008, issues of financial scams and unscrupulous lending, misconduct on Wall Street, and the financial capability of consumers garnered significant attention from policymakers, regulators, and advocates. The Department of Justice's numerous settlements with financial institutions since the financial crisis speak to the extreme levels of misconduct rampant within the financial services sector.

The sharp focus led to positive results in 2010 when the Dodd-Frank Wall Street Reform and Consumer Protection Act was signed into law. Dodd-Frank created the Consumer Financial Protection Bureau (CFPB), which is focused on protecting the interests of consumers. The CFPB has introduced several important protections for Hispanic consumers, including a remittance rule that went into effect in October 2013 and nationwide mortgage servicing standards that went into effect in January 2014.

NCLR's research and policy work over the years has documented gaps and limitations in social safety nets and work-support systems that overlook too many working families. NCLR has published the following original research related to the financial conditions of Latino families:

- *Latino Financial Access and Inclusion in California*
- *Banking in Color: New Findings on Financial Access for Low- and Moderate-Income Communities*

In addition, NCLR has submitted the following statements for the record:

- "Putting an End to the Foreclosure Crisis for Latinos and Communities of Color"
- "Principles to Modernize the Community Reinvestment Act: How CRA Can Help Low-Income Latino Families Build Wealth and Secure Their Financial Future"
- "Harnessing the Power of the Community Reinvestment Act to Connect Latinos to Banking Services"

NCLR also participated in the Bipartisan Policy Center's Financial Regulatory Reform Initiative and co-authored a report titled *The Consumer Financial Protection Bureau: Measuring the Progress of a New Agency*.

Given the significant existing racial and ethnic disparities in access to mainstream financial services, Blacks and Hispanics have few choices when seeking products and safety services to meet their financial needs. This means that nonbank credit products can substantially impact the household balance sheets of Latinos and other minority consumers.

Today, the most ubiquitous providers of these alternative financial products are payday loan lenders, nationally numbering more storefronts than McDonald's and Starbucks combined.[1] A recent study released by the Center for Responsible Lending found that race and ethnicity are the leading factors in determining payday lender locations, with concentrations of these businesses in lower-income and largely minority communities.[2]

Payday loans are inherent debt traps, locking borrowers in a cycle of rollover loans that can last several months and ultimately cost hundreds of dollars in interest. According to testimony before the Senate Committee on Banking, Housing, and Urban Affairs, more than 58% of payday loan borrowers report using the loans to cover monthly expenses such as utilities, rent, and food.[3] However, a payday loan used to cover these basic expenses will usually require a balloon payment averaging $400 from a borrower's next paycheck. This results in a pattern for countless borrowers who pay off their loan and then must immediately take out another loan to continue covering their living expenses. This revolving door of loans creates a debt trap that can leave a borrower in a worse financial position than before they took out the original loan. Regulations are needed to protect consumers from these harmfully designed and largely unchecked financial products.

The payday lending marketplace is not a small segment of consumers: research shows that 12 million Americans take out a payday loan each year. Of these consumers, four out of five are not able to pay it back within the original loan term,[4] suggesting that the loan is not affordable for the majority of consumers who use them. While there is a definite need for small-dollar credit and loans, especially for low-income consumers and those who may be outside the financial mainstream, consumers should not end up in financial ruin as a result of taking out a loan. The CFPB recognizes that a crucial principle—the ability to repay a loan—must apply to a

sufficiently broad range of small-dollar loans, not just a narrowly defined set of payday or car-title loans. The proposed rule released by the CFPB in late March is a huge step forward in the right direction—providing much-needed protections for products that have gone unregulated for far too long.

Thankfully, consumers now have a federal agency dedicated to monitoring and regulating toxic financial products such as payday loans. The CFPB recognizes the importance of addressing the harmful nature of payday loans. NCLR welcomes these efforts to reduce household debt and help Latino families and other consumers continue recovering from the economic crisis, and we stand ready to work with CFPB as it takes action on this issue.

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[1] Federal Reserve Bank of St. Louis, *Payday Loans: Time for Review* (St. Louis, MO: Federal Reserve Bank of St. Louis, 2014), https://www.stlouisfed.org/publications/inside-the-vault/fall-2014/payday-loans (accessed April 14, 2015).
[2] Wei Li, et al., *Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California* (Washington, DC: Center for Responsible Lending, 2009).
[3] Senate Committee on Banking, Housing, and Urban Affairs, Subcommittee on Financial Institutions, *Are Alternative Financial Products Serving Consumers?*, 113th Cong., 2nd sess., 2014.
[4] Susanna Montezemolo, *The State of Lending in America and its Impact on U.S. Households*, (Washington, DC: Center for Responsible Lending, 2013).