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# As Legal Winds Shift, so Should Your Business

**By preparing for recent and impending changes, brokers can avoid trouble**

**T**he regulatory and legislative landscape of 2010 was as challenging as it ever has been. The past two years brought an onslaught of regulatory, legal, agency and investor changes.

As we enter 2011, even more significant regulatory and legislative changes loom. By looking deeper at some of these and their likely effects, mortgage brokers and loan originators can prepare for what's next.

## The S.A.F.E. Act

The effects of the Secure and Fair Enforcement for Mortgage Licensing Act (aka the S.A.F.E. Act) are still being felt across the industry and especially by mortgage brokers. Although some loan originators are exempt from testing requirements, nondepository lenders — including brokers — must undergo state and national licensure testing.

Fulfilling their testing obligations imparts disproportionate time, money and management obligations on brokers. Not only is this unfair, but it also leads consumers into an environment where a large portion of the industry remains unlicensed.

A lack of uniformity in licensing requirements among states and institutions exists. Rather than accept this, brokers should promote a single national uniform standard that applies to all mortgage-providers. The result would be better for consumers and would lead to less fraud, more professionalism and increased consumer confidence.

In the meantime, brokers must comply with all licensing rules. In some cases, this will mean giving up time that would otherwise be spent helping clients and originating loans.

## Risk retention

The Dodd-Frank Wall Street Reform and Consumer Protection Act requires 5-percent risk retention for any loans other than low-risk loans. The technical term the law uses to describe low-risk loans is “qualified residential mortgages,” which are yet to be defined by regulations.

Currently, loans insured by the Federal Housing Administration or guaranteed by the U.S. Department of Veterans Affairs are exempt from this retention requirement. Loans in securities backed by Fannie Mae and Freddie Mac aren't, although depending upon their terms, they may be exempt as qualified residential mortgages.

Brokers should pay attention and prepare for when these changes become law. As liquidity and recordkeeping requirements for nonagency loans change, non-qualified residential mortgages will likely become tremendously expensive to execute. This could be avoided if regulators put the onus on securitizers, which in turn didn't pass down costs.

Even for qualified residential mortgages, brokers must understand the final rules. Those who don't risk operating improperly. One question brokers will be interested in having answered is this: Will regulators apply

exemptions on a per-loan-product basis?

As risk retention makes its way from concept to law, it seems likely that sub-prime and Alt-A lending will be more difficult than ever. Many brokers who once produced those loans may stop, thus avoiding risk while sacrificing market share and limiting consumer choice.

## Compensation

Major changes in broker compensation also loom. Under the final rule issued recently by the Federal Reserve Board, compensation prohibitions will apply to mortgage brokers, broker companies, and loan-officer employees of mortgage brokers and mortgage bankers — but not to mortgage bankers themselves.

Generally speaking, beginning this coming April 1, the parties noted can't be compensated based on a loan's rate or terms other than the loan amount. They also may receive compensation from lenders or consumers, but not both.

As of press time, on the other hand, mortgage brokers could be paid based on interest rate, loan type and from multiple parties. All that will change, and brokers would be wise to start discussing future compensation plans with their lenders.

Brokers who previously have originated few loans but generated high revenues based on interest rate, loan type or fees

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from multiple parties must change their strategies to protect their income. With few exceptions, it will no longer be possible to earn a large income without originating a large volume of loans.

### **New bureau**

The Consumer Financial Protection Bureau emerged from the Dodd-Frank Act. By law, the bureau will be established in 2011 and will be able to rewrite regulations. It also will supervise and bring enforcement actions against banks and nonbanks.

Until the bureau gets up and running, it's difficult to know how it will work with

various segments of the industry or with other regulators, and what issues it will focus on. It seems certain, however, that fair lending will be at or near the top of its list.

The agency will have broad powers to define and enforce violations of unfair, deceptive or abusive lending practices. Such power could put brokers and lenders in a precarious position.

Brokers can avoid Consumer Financial Protection Bureau scrutiny by originating good loans for well-qualified consumers. Unfortunately, the market for less-than-ideal borrowers could continue to shrink as brokers and lenders seek to avoid legal

trouble that might not emerge until years after loans have closed.

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As we approach 2011, many brokers likely will think hard about their decision to continue in the business. Those who carry on will do so in an environment with limited compensation and increased liability. Although economic survival won't come easy, those who prepare early can stay ahead of the curve, avoid legal run-ins and build market share by helping consumers, real estate agents and others navigate the changing regulatory and legislative winds. ●