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REDUCE MORTGAGE BROKER DEPOSIT AMOUNT

House Bill 5737 as introduced
First Analysis (6-14-88)

Sponsor: Rep. Roland G. Niederstadt
Committee: Corporations and Finance

THE APPARENT PROBLEM:

The Mortgage Brokers, Lenders, and Servicers Licensing Act was created last year in response to the Diamond Mortgage scandal of 1986 in which investors lost millions of dollars, apparently due to unscrupulous servicing of mortgage loans. The act requires those applying to be licensed as mortgage brokers or lenders to submit proof of financial responsibility, in the form of a surety bond, letter of credit or similar note of security, in the amount of $25,000 to the Financial Institutions Bureau (FIB) — the administrator of the act. When the act was created, the bureau felt the $25,000 security requirement would not be too high for most smaller companies wishing only to broker or make a limited number of low-cost mortgage loans. The bureau, however, after administering the act for the past year, apparently has received complaints from a number of smaller firms who would like to offer limited mortgage services but are finding it difficult to raise this initial amount. In fact, the act's original intent apparently was to regulate the largest mortgage companies that service a greater number of and larger dollar amounts in mortgage loans. (Those applying to be licensed as "mortgage servicers" under the act must submit a $100,000 security note.) Some have even suggested that such smaller lenders or brokers should not even be required to post the bond, in certain cases, since they present little danger to borrowers. Because the current bond amount reportedly has discouraged smaller firms from entering the first mortgage market, which has reduced competition within the industry, some feel the act's bonding requirements for certain broker and lender applicants should be eased.

THE CONTENT OF THE BILL:

The bill would amend the Mortgage Brokers, Lenders, and Servicers Licensing Act to reduce the required deposit amount for a person applying to be licensed as a mortgage broker or lender from $25,000 to $15,000. (The bill would not affect those applying to be licensed as a "mortgage servicer," who are required to submit a $100,000 surety deposit.) In place of a surety bond or letter of credit the act allows a license applicant to submit, among other things, a true copy of the corporate surety bond the applicant is required to maintain in order to service mortgage loans on behalf of the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC), or the Government National Mortgage Association (GNMA). The bill would delete this as an option for showing proof of financial responsibility.

In addition, the bill specifies that a mortgage broker would be exempt from the provision regarding the submission of proof of financial responsibility if he or she had deposited all funds received from a prospective borrower into an escrow account and did not possess or control the funds associated with the loan application prior to the closing or denial of the mortgage loan. The bill would not prohibit the disbursement of funds by the escrow agent to third parties for the actual cost of a property appraisal and credit report in connection with a mortgage loan application. An escrow account that was created as specified in the bill would have to be established in a manner approved by the commissioner and deposited only in a federally insured depository financial institution (a bank, savings and loan, or credit union).

MCL 445.1654

FISCAL IMPLICATIONS:

According to the Financial Institutions Bureau of the Department of Commerce, the bill would have minor fiscal implications due to a small increase in the number of firms that would have to be examined by the department. (6-9-88)

ARGUMENTS:

For:

The act's original intent was to balance the need for better regulation of mortgage companies with a need to preserve a healthy, competitive and growing industry. Bigger firms licensed as mortgage "servicers" have to prove greater financial responsibility by submitting $100,000 surety upon application. The need to regulate smaller brokers and lenders apparently is not as great. In fact, the initial bonding amount of $25,000 suggested by the FIB was an arbitrary figure which the bureau realized could be subject to alteration after some time if necessary. After one year of enforcing the act, the bureau apparently feels the amount is too high and, in some cases, may not be necessary at all. Reducing the bond amount, or in some cases reducing the requirement to show financial proof at all, will encourage more firms to enter the first mortgage market, thereby improving competition among firms and, ultimately, saving borrowers money. The bill, however, would not alter the bureau's responsibility to monitor firms — both annually and on an irregular basis — and, if necessary, punish licensees.

Against:

Why decrease the safety factor currently extended to those with any amount of money tied up in a mortgage contract? After the heartache and embarrassment caused by the Diamond Mortgage scandal, where investors and borrowers lost huge sums of money, it seems foolish to relax laws intended to protect against similar improprieties. Does it matter whether a person is cheated by a small operator rather than a large one? If anything, the act should provide stiffer licensure requirements and penalties.

Response: The bureau feels the act provides enough protection for borrowers and investors by requiring that all

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licensees are monitored on a regular and irregular basis. The bonding requirement defeats the need to allow smaller firms to easily enter the market — additional firms that could increase healthy competition within the industry and actually save consumers money.

POSITIONS:

The Financial Institutions Bureau supports the bill. (6-8-88)

The Michigan Association of Realtors has no position on the bill. (6-8-88)

The Michigan Bankers Association has no position on the bill. (6-8-88)