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Senate Fiscal Agency

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House Bill 4701 (Substitute S-3 as reported)

House Bill 4702 (Substitute S-1 as reported)

House Bill 4703 (Substitute S-1 as reported)

Sponsor: Representative John Bennett

House Committee: Corporations and Finance

Senate Committee: Commerce and Technology

Date Completed: 10-23-87

## RATIONALE

Recently, some companies doing business in mortgages in Michigan are reported to have engaged in unscrupulous practices. The most notorious example is that of Diamond Mortgage and A.J. Obie and Associates, two firms under the same ownership, with the first making mortgage loans and selling those loans to investors brought in by A.J. Obie. Allegedly, as the firms began to collapse late last year, it became apparent that often a single mortgage concurrently had been sold to more than one investor and that although Diamond had been receiving investors' funds, it was not disbursing that money to borrowers. Losses to investors have been estimated at roughly \$50 million; borrowers reportedly lost an incalculable sum in the form of clouded titles and exorbitant fees. Both firms are in Chapter 7 (liquidation) bankruptcy, and the principals recently pleaded "no contest" to criminal charges of securities fraud.

The Diamond Mortgage experience has highlighted a need for comprehensive State oversight of first mortgage transactions. Depository institutions, secondary mortgage lenders, real estate brokers, and securities broker-dealers all are regulated by State law, but State officials note that there is no single locus of responsibility for overseeing those in the business of making, brokering, or servicing first mortgage loans. Some contend that legislation should be enacted to ensure that adequate authority to monitor and regulate first mortgage lending is vested in a single agency.

## CONTENT

House Bill 4701 (S-2) would create the "Mortgage Brokers, Lenders, and Servicers Licensing Act" to regulate those who act as brokers, makers, or servicers of first mortgage loans or land contracts on Michigan property designed for occupancy by four or fewer families. House Bills 4702 and 4703 would amend the Occupational Code and the Uniform Securities Act, respectively, to exempt certain people from those Acts, if they were licensed or registered under the "Mortgage Brokers, Lenders, and Servicers Licensing Act" proposed by House Bill 4701.

The bills are tie-barred.

### House Bill 4701 (S-1)

The bill would create the Mortgage Brokers, Lenders, and Servicers Act, and would do all of the following:

- Specify licensing and registration requirements for mortgage brokers, mortgage lenders, and mortgage servicers.
- Specify the terms and processes for the surrender, suspension, and revocation of a license or registration.
- Require the Commissioner of the Financial Institutions Bureau (FIB) to supervise and control mortgage brokers, mortgage lenders, and mortgage servicers doing business in Michigan.
- Specify the procedures for complaints and investigations of alleged violations of the bill.
- Specify record keeping requirements for licensees and registrants.
- Provide a list of actions that would be considered violations of the proposed Act.
- Specify persons and institutions that would be exempt from the proposed Act.
- Provide penalties for violations of the proposed Act.
- Include other provisions with regard to fees received under the proposed Act, allowable charges that a licensee or registrant could require a borrower to pay, disclosure requirements of a mortgage servicer, and the validity and enforceability of mortgage loans.

### Licensing and Registration

The bill would prohibit any person from acting as a mortgage broker, lender, or servicer without obtaining a license from, or registering with, the Commissioner of the FIB, unless the person performed services solely as a full-time employee of a mortgage broker, lender, or servicer or specifically was exempted under the bill.

Licensing. Applications for licensure or renewal of licensure would have to be made in writing on a form prescribed by the Commissioner. After an investigation, the Commissioner would have to issue or renew a license if he or she determined "that the experience, character, business reputation, and general fitness of the applicant and its officers, directors, shareholders, partners, and affiliates command the confidence of the public and warrant the belief that the applicant and its officers, directors, shareholders, partners, and affiliates will comply with the law, and that grounds for revoking, suspending, or denying a license" did not exist.

An applicant who acted solely as a mortgage broker and received funds from a prospective borrower prior to the mortgage closing or solely as a mortgage lender would

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have to deposit with the Commissioner \$25,000 as proof of financial responsibility; applicants who did not act solely as a mortgage broker or lender would have to deposit \$100,000. The deposit could be in the form of either a corporate surety bond that was payable to the Commissioner and expired no earlier than the license, or an irrevocable letter of credit upon which the applicant was the obligor, which expired no earlier than the license and was issued by a Federally-insured depository institution. The bond or letter of credit would be conditioned upon the conduct of the business with regard to the bill's requirements and rules promulgated by the Commissioner. Rather than a bond or letter of credit, an applicant could furnish one of the following as proof of financial responsibility:

- Obligations of the United States, or obligations that were guaranteed fully by the United States, or any general obligations of any State or political subdivision of the United States, with a maturity date of three years or less, in an amount of at least that of the bond requirement. (Obligations would be deposited with the State Treasurer under terms prescribed by the Commissioner, and earned interest would accrue to the applicant's account.)
- A certificate of deposit of a Federally-insured financial institution with a maturity date of three years or less, in an amount at least that of the bond requirement, which was not available for withdrawal except by direct order of the Commissioner. (Certificates of deposit would be deposited with the State Treasurer under terms prescribed by the Commissioner, and earned interest would accrue to the applicant's account.)
- A "true copy" of the corporate surety bond that the applicant was required to maintain to service mortgage loans on behalf of the Federal national mortgage association, the Federal home loan mortgage corporation, or the government national mortgage association. (Corporate surety bonds would have to be delivered to the Commissioner.)

The Commissioner could reduce, waive, or modify the proof of financial responsibility requirements for a mortgage servicer who serviced up to 300 land contracts or mortgages and did not collect and maintain money for the purpose of paying taxes or insurance on the contract or mortgage.

Licensees who would act solely as mortgage brokers and would receive funds from prospective borrowers prior to a mortgage loan closing or those who would act solely as mortgage lenders would be required to have a minimum net worth exceeding \$25,000 determined by the Commissioner. Other licensees would have to have a minimum net worth not exceeding \$100,000. A broker or lender who acted as a mortgage servicer would have to have a net worth of at least \$100,000. "Net worth" would be determined at the conclusion of the fiscal year preceding the date of application for licensure or renewal and would be computed in accordance with generally accepted accounting principles. The following assets, however, would be excluded from the computation of net worth:

- Portions of assets pledged to secure obligations of persons or entities other than the applicant.
- Assets, except construction loans receivable, secured by first mortgages from related companies, due either from officers or stockholders of the applicant, or from persons in which the applicant's officers and stockholders have an interest.
- Amounts in excess of the cost or market value of mortgage loans in foreclosure, or real property acquired through foreclosure, whichever was less.

- Investments in joint ventures, subsidiaries, or affiliates that are greater than the market value of the assets.
- Good will or value placed on insurance renewals or property management contract renewals or similar intangible value.
- Organization costs.

The bill specifies that a license would expire on June 30 of each year. A license could be renewed, however, by filing an application for renewal and paying the succeeding year's annual fee. Renewal applications and fee payments would have to be received by the Commissioner on or before June 15 of each year. Applicants filing for initial application, or for a first application after a suspension or revocation, would have to pay to the Commissioner a fee of \$200 for the cost of the required investigation, and a \$300 annual fee. Renewal application fees would be \$300.

The bill would prohibit the transfer or assignment of a license without the Commissioner's consent. The sale, transfer, assignment, or conveyance of more than 25% of the outstanding stock of a licensee that was a corporation, or more than 25% of the interest in a licensee that was a partnership or other unincorporated association, would be considered to be a transfer of the license.

No more than 75 days after the close of a licensee's fiscal year, the licensee would have to deliver to the Commissioner a financial statement for the fiscal year that was prepared from the licensee's books and records. The statement could be in any of the following forms:

- A form prescribed by the Commissioner.
- A report, similar to the form prescribed by the Commissioner, represented by the licensee to be "true and complete".
- A format prepared and certified by an independent certified public accountant who was licensed by a regulatory authority of any State or political subdivision of the United States.

Registration. The bill would require all of the following to register with the Commissioner:

- A mortgage broker, lender, or servicer approved as a seller or servicer by the Federal national mortgage association or the Federal home loan mortgage corporation.
- A mortgage broker, lender, or servicer approved as an issuer or servicer by the government national mortgage association.
- A mortgage broker, lender, or servicer licensed to make regulatory loans pursuant to the Regulatory Loan Act, or licensed to make secondary mortgage loans pursuant to Public Act 125 of 1981.
- A real estate broker or salesperson licensed under Article 25 of the Occupational Code who acts as a mortgage broker for not more than one licensee or registrant, or who acts as a mortgage broker, lender, or servicer only in connection with real estate sales engaged in by an affiliated real estate broker, and who receives additional compensation beyond the customary commission on real estate sales. ("A real estate broker or real estate salesperson, in connection with real estate sales in which the real estate broker or real estate salesperson affiliated with the real estate broker is engaged, who acts as a mortgage broker on 10 or fewer mortgage loans in any 12-month period from July 1 to June 30 and who receives for such services additional compensation beyond the customary commission on real estate sales", however, would be exempt from registration or licensing for that 12-month period.)

Registrants would not be required to comply with the licensure provisions of the bill and would not be subject to annual examination by the Commissioner or be required to file annual reports with the Commissioner. Registrants would be required to pay the \$300 annual fee, however, and would be subject to the same renewal requirements as licensees.

A mortgage broker, lender, or servicer that was a subsidiary or affiliate of a depository financial institution, or of a holding company of a depository financial institution, would not be subject to the bill's misdemeanor violation provisions regarding the transfer or assignment of a mortgage loan or a security directly representing an interest in one or more mortgage loans. Such a broker, lender, or servicer, however, could register and become subject to the bill's provisions applicable to registrants.

#### Surrender, Suspension, and Revocation

Under the bill, a licensee or registrant could surrender a license or registration by delivering it, with a written notice of surrender, to the Commissioner. The surrender of a license or registration would not affect a proceeding seeking suspension or revocation. Surrender, suspension, or revocation of a license or registration would not affect the licensee's or registrant's civil or criminal liability for acts committed prior to surrender, suspension, or revocation, and could not impair or affect the licensee's or registrant's obligations under a preexisting contract.

Notice of intention to enter an order of license or registration suspension or revocation, or notice to an applicant of refusal to issue a license, would have to be in writing and served personally or by certified mail. Within 20 days after such notice, the licensee, registrant, or applicant could request a hearing to contest the order or refusal. If no hearing were requested, the Commissioner would have to enter a final order of suspension or revocation. Hearings would have to be conducted in accordance with the Administrative Procedures Act.

#### Supervision and Control

The bill specifies that the Commissioner would be responsible for the general supervision and control over mortgage brokers, lenders, and servicers doing business in Michigan. The Commissioner would be granted the power to do all of the following:

- Promulgate "reasonable" rules pursuant to the Administrative Procedures Act, as necessary to implement and administer the proposed Act.
- Deny application for licensure; suspend or revoke a license or registration; and conduct examinations and investigations as necessary for the efficient enforcement of the bill and rules promulgated under it.
- Advise the Attorney General and county prosecutors that he or she believed a licensee, registrant, or other person was violating the proposed Act, and the Attorney General or prosecutor would have to take the appropriate legal action to enjoin the business's operation or prosecute violations.
- Bring an action in the Ingham County Circuit Court in the name of the State against a licensee, registrant, or other person who participated in, or was about to participate in, an unsafe or injurious practice or act in violation of the bill or a rule promulgated under it, to enjoin the person from continuing the practice or engaging in the act.
- Order a person to cease and desist from a violation of the bill or a rule promulgated under it; or censure a licensee or registrant.
- Require that restitution be made in accordance with the bill; and assess civil fines in accordance with the bill.

#### Complaints and Investigations

The bill specifies that the Attorney General, the Commissioner, or any other person could file a complaint with the Commissioner alleging a violation of the proposed Act, a rule promulgated under it, or an order issued under it. If the complaint were made by the Commissioner, he or she would have to designate one or more FIB employees to act as the complainant. The Commissioner could begin an investigation upon receipt of a complaint. If a complaint were received against a registrant who was a subsidiary of a Federally-chartered depository financial institution, a copy of the complaint would have to be sent to the appropriate Federal regulatory agency. The Commissioner would be required to attempt to determine the disposition of the complaint, but could not investigate if the complaint were being pursued adequately by the Federal agency.

If an investigation were conducted, the employees or agents of the FIB would be required to complete the investigation "within a reasonable period of time". If the investigation failed to uncover evidence of a violation, the complaint could not be used in subsequent decisions pertaining to the issuance, renewal, suspension, or revocation of a license or registration of the person against whom the complaint was filed. The results of the investigation would have to be forwarded both to the complainant and the person against whom the complaint was filed. If the investigation did disclose evidence of a violation, however, the Commissioner or the Attorney General could prepare a formal complaint to be served on the person against whom the complaint was made, in addition to other action authorized by law. A copy of the formal complaint also would have to be provided to the complainant.

Upon the completion of an investigation, the Commissioner could issue an order summarily suspending a license or registration pursuant to Section 92 of the Administrative Procedures Act (APA) "based on an affidavit by a person familiar with the facts set forth in the affidavit or, if appropriate, based upon an affidavit, on information and belief, that an imminent threat of financial loss or imminent threat to the public welfare exists". Also pursuant to Section 92, an administrative law hearings examiner would have to grant a request to dissolve a summary suspension order unless he or she found that an imminent threat of financial loss or imminent threat to the public welfare existed and required emergency action and continuation of the summary suspension order. The record of the summary suspension hearing would have to become part of the record on the complaint at a subsequent hearing in a contested case.

After an investigation, the Commissioner could issue an order to cease and desist from a violation of the proposed Act, or a rule promulgated or order issued under it. A person ordered to cease and desist would be entitled to a hearing, if he or she filed a written request within 30 days. Hearings would have to be conducted in accordance with the APA. A violation of a cease and desist order would be a violation of the bill and the Commissioner or the Attorney General could take appropriate action in the Ingham County Circuit Court to restrain and enjoin the person from further violation of the cease and desist order. The bill specifies that a summary suspension order, cease and desist order, or injunctive relief issued in relation to a licensee would be in addition to an informal conference, criminal prosecution, or proceeding to deny, revoke, or suspend a license or registration, or any other legal action.

After an investigation and formal complaint, the Commissioner would have to serve a notice of hearing pursuant to Section 71 of the APA upon the person against

whom the complaint was filed and the complainant. Also required to be served at that time would be a notice of an opportunity to settle the complaint through an informal conference. Either of the parties who had been served notice of a hearing could request, within 15 days, an opportunity to settle the complaint in an informal conference. Such a proceeding could be held only if the person against whom the complaint was filed agreed to the conference; if a conference were held, the hearing would be postponed. An informal conference could result in a settlement, consent order, waiver, default, or other method of settlement agreed upon by the person complained against and the Commissioner. A settlement could include a license or registration revocation or suspension, restitution, or a penalty provided for in the bill. If an informal conference were not held, or did not result in a settlement, a hearing would have to be held as provided in Chapter 4 of the APA.

The bill specifies that there is nothing in the proposed Act to prevent a person against whom a complaint had been filed from demonstrating compliance with the bill, a rule promulgated under it, or an order issued under it. In addition, the bill would not preclude a person whose license or registration had been suspended or revoked from continuing to service mortgage loans pursuant to contracts in existence at the time of suspension, for a period of up to six months after the final decision of the presiding officer in the contested case hearing that resulted in the revocation. Further, nothing in the bill would preclude a person whose license or registration had been suspended or revoked from making a mortgage loan pursuant to a commitment to make a mortgage loan issued prior to the suspension or revocation. A person who received a commitment issued by someone whose license or registration was suspended or revoked, however, could, prior to closing the loan, terminate the commitment and receive a refund of all money paid to the person whose license or registration was suspended or revoked.

In the conduct of any examination or investigation under the proposed Act, the bill specifies that the Commissioner could do any of the following:

- Subpoena any person; administer oaths; and interrogate any person under oath concerning the business and conduct of affairs of any person subject to the provisions of the bill, and require the production of books, records, or papers relative to the inquiry.
- During regular business hours, have free access to the offices, places of business, or other location where the licensee or registrant, or an affiliate maintained business-related documents, and to the books, accounts, papers, records, files, documents, safes, and vaults of a licensee or registrant.
- Employ independent investigators to conduct part or all of the investigation, in the case of an investigation other than the annual examination.

Information obtained during an investigation or examination would be confidential and could not be available for public inspection or copying, or divulged to any person, except as follows:

- To the Attorney General or any regulatory agency.
- In connection with an enforcement action brought pursuant to the bill or an applicable Act.
- Under subpoena, to any party in a private action.
- To law enforcement officials or persons authorized by the Ingham County Circuit Court to receive the information.

Persons subpoenaed who willfully refused or neglected to appear at the time and place named in the subpoena; or to produce books, accounts, records, files, or documents required by the Commissioner; or who refused to be sworn

or, unless permitted by law, to answer as a witness, would be guilty of a misdemeanor under the bill.

The Commissioner could only conduct one examination of a licensee in any 12-month period from July 1 to June 30. The cost of one examination of a licensee would be assessed annually to the licensee. In addition, the Commissioner could conduct an investigation of a licensee or registrant against whom a complaint was filed, but the licensee or registrant would have to pay the cost only if he or she repeatedly violated a "material" provision of the proposed Act. The fee for an examination or investigation could be up to \$20 per hour, but not more than \$40 per hour for each examiner involved in the examination. The fee also could include the "actual and reasonable" travel, lodging, and meal expenses of authorized examiners, when traveling out of State, and the cost of independent investigators. The Commissioner would be required to cooperate with other agencies of the State or Federal government, other states, the Federal national mortgage association, or the Federal home loan mortgage corporation, and would have to accept examinations of those entities in connection with, or in place of, an examination by the Commissioner. The Commissioner could still undertake an investigation if he or she determined that the examinations were not available or did not provide the necessary information to enable the Commissioner to fulfill his or her responsibilities. The Commissioner would have to attempt to examine the books and records summarizing any other activity in which the licensee was engaged, pursuant to other statutes that grant the Commissioner regulatory responsibility over the licensee.

#### Record Keeping

The bill would require licensees and registrants "to maintain books, accounts, records, and documents of the business, as may be prescribed by the commissioner, conducted under the license or registration to enable the commissioner to determine whether the business of the licensee or registrant is conducted in accordance with this act and the rules promulgated under this act". Photocopies of the records would satisfy this requirement. If the pertinent records were not available in Michigan, the licensee or registrant would have to pay the "reasonable" travel expenses of the examiner.

The licensee or registrant would be required under the bill to preserve and make available for examination each mortgage loan document in its possession or control until the mortgage loan was transferred or assigned, or three years after the closing of the mortgage loan, whichever was first. This requirement would include, "by way of example and not limitation", the application, employment verification, credit report, and loan disclosure statement and settlement statement. If the loan were assigned or transferred, the licensee or registrant would have to preserve and keep copies of the promissory note, mortgage, land contract, truth-in-lending disclosure statements, and settlement statements in its possession or control for three years after the date of the transfer or assignment. All documents pertaining to a rejected application for a mortgage loan would have to be preserved and kept for the length of time required by State or Federal law. All other books, records, accounts, and documents pertaining to a licensee's business would have to be preserved and kept available for examination for at least three years after the end of the relevant fiscal year.

Annually, licensees would have to file a report with the Commissioner giving information concerning the licensee's business and operations during the preceding calendar year. The Commissioner also could require a licensee or registrant to file special reports as he or she considered necessary for supervision under the proposed Act. All

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required reports would have to be signed and affirmed. A person who willfully and knowingly subscribed and affirmed a false statement in a required report would be guilty of a felony, punishable by imprisonment for not more than 15 years.

#### Violations

It would be a violation of the proposed Act if a licensee or registrant did any of the following:

- Did not conduct business according to law, or had violated the proposed Act or a rule promulgated or order issued under it.
- Engaged in fraud, deceit, or material misrepresentation in connection with any transaction governed under the proposed Act.
- Repeatedly failed to provide borrowers with material disclosures of information as required by State or Federal law, either intentionally or due to gross or wanton negligence.
- Suppressed or withheld information from the Commissioner that was in the possession of the licensee or registrant and would have resulted in ineligibility for licensure or registration.
- Violated any provision of Public Act 125 of 1966, which regulates the handling of mortgage escrow accounts by mortgagees.
- Failed to place in escrow money, funds, deposits, checks, drafts, or other negotiable instruments entrusted to the mortgage broker, lender, or servicer; or failed to deposit and retain the funds in a trust or escrow account with a Federally-insured depository institution.
- Refused to permit an examination of the licensee's or registrant's books and affairs, or refused or failed to furnish information to make a required report.
- Was convicted of a felony or misdemeanor of which an essential element is fraud.
- Refused or failed to pay expenses assessed under the bill.
- Failed to make restitution or pay damages as ordered by the Commissioner, an administrative agency, or a court.
- Failed to make a mortgage loan pursuant to and in accordance with, a written commitment do so, when the mortgagee had satisfied the conditions of the commitment.

The bill also specifies several actions that would be misdemeanor violations. Such violations could result in a fine of up to \$5,000 or imprisonment for up to three years, or both. A person who engaged in the business of a mortgage broker, lender, or servicer without a license would be guilty of a misdemeanor as would someone who transferred or assigned a mortgage loan or a security directly representing an interest in one or more mortgage loans prior to the disbursement of 75% or more of the proceeds of the loan to or for the benefit of the borrower. (The above violation would not apply to land contracts not considered to be an equitable mortgage.) If one of the following applied, a mortgage loan or security representing an interest in one or more mortgage loans could be transferred or assigned to an individual investor without being considered a misdemeanor:

- The transfer or assignment was made through a broker-dealer that was a member of the New York stock exchange.
- The transfer or assignment was made through a broker-dealer who was licensed under the Uniform Securities Act and was not affiliated with the mortgage dealer unless the broker-dealer acquired his or her license prior to September 1, 1987, and had continuously

maintained that license subsequent to September 1, 1987, and the broker-dealer acquired the mortgage loan or security on a firm commitment.

- The transfer or assignment was made to a person whom the transferor or assignor believed was a business entity having either after tax net income of at least \$100,000 in its last fiscal year or a net worth of at least \$1,000,000 at the time of purchase.
- The transfer or assignment was made to a person whom the transferor or assignor believed had an investment of more than \$50,000 in such loans and securities, including installments to be paid within one year after the purchase; or had either personal income, before taxes, of at least \$100,000 for the last fiscal year or net worth of at least \$1,000,000, was capable of bearing the economic risk, and had the knowledge and experience in financial and business matters necessary to evaluate the merits and risks of the prospective investment or had obtained the necessary advice to do so.
- A transferor or assignor did not maintain its principal place of business in Michigan and the transferee or assignee neither was a resident of Michigan nor maintained its principal place of business in this State.

#### Exemptions

The proposed Act would not apply to any of the following:

- Depository financial institutions.
- Residential builders and their salespersons, when transactions are made or negotiated in connection with the sale of a residential structure constructed by that builder.
- A real estate broker or salesperson who only acts as a mortgage broker in connection with a real estate sale or lease and without additional compensation beyond customary commissions, or a salesperson who receives additional compensation only from a real estate broker for which the salesperson is an agent or employee.
- A home improvement installment contract entered into by a home improvement contractor.
- Agencies or corporate instrumentalities of the United States and of this State and its political subdivisions.
- A mortgage lender or servicer that makes or services 10 or fewer loans in a 12-month period from July 1-June 30.
- An individual licensed to practice law in Michigan and not engaged in negotiating loans secured by real property, when services are rendered in the course of the individual's law practice.
- A person who makes mortgage loans exclusively for the benefit of employees, if the proceeds of the loan are used to assist the employee in meeting housing needs.
- A person acting as a fiduciary with respect to any employee pension benefit plan qualified under the Internal Revenue Code who makes mortgage loans solely to plan participants from plan assets.
- A mortgage broker, lender, or servicer that is a subsidiary or affiliate of a depository financial institution, or holding company of such an institution.

#### Penalties

If the Commissioner found that a licensee or registrant had violated the bill or rules promulgated under it, he or she could assess a civil fine of not more than \$1,000 for each violation up to \$10,000 for infractions resulting from a single transaction. The costs of investigation also could be assessed. The Commissioner also could suspend or revoke a license or registration or refuse to issue or renew a license. The civil fine could be sued for by the Commissioner and could be collected and enforced by summary proceedings by the Attorney General. Each individual injured by a violation would constitute a separate violation. (These penalties would not apply to a violation that resulted

from a bona fide error.) In making his or her determination, the Commissioner would be required to consider the extent to which the violation was a knowing and willful violation, the extent of the injury suffered because of the violation, the corrective action taken by the licensee or registrant to ensure that the violation would not be repeated, and the record of the licensee or registrant in complying with the bill.

Violators would be required to make restitution to each individual injured by the violation. The violator's license or registration could be suspended until restitution was made.

The bill states that any person could bring an action to obtain declaratory judgment that a method, act, or practice was a violation of the proposed Act; obtain an injunction against a person engaged in, or about to engage in, a method, act, or practice that violated the proposed Act; recover actual damages resulting from a violation of the bill, or \$250, whichever was greater, together with reasonable legal fees. If the licensee or registrant established by a preponderance of the evidence that failure to comply with the bill was not willful, intentional, or the result of gross or wanton negligence, amounts recovered could not exceed actual damages.

If the Commissioner determined that a licensee or registrant intentionally, or as a result of gross or wanton negligence, was not servicing mortgage loans according to the terms of the proposed Act or the terms of the servicing contracts, the Commissioner could appoint a conservator for the licensee or registrant. The Commissioner could require the conservator to produce a bond and security as he or she considered proper. The conservator could be one of the FIB examiners or another competent and disinterested person. The FIB would have to be reimbursed out of the assets of the conservatorship for actual expenses. Conservators would be considered employees of the FIB. A conservator's expenses would have to be paid out of the assets of the licensee or registrant, upon the approval of the Commissioner. Expenses of the conservator would be a first charge and would have to be paid fully before final distribution or payment of dividends was made to creditors or shareholders.

Under the direction of the Commissioner, a conservator would take sole control of the affairs of the licensee or registrant. The licensee or registrant could transfer or assign the rights to service mortgage loans to a person approved by the Commissioner. The conservator would be responsible for assuring that mortgage loans were serviced in accordance with the bill and servicing contracts.

The Commissioner could terminate the conservatorship and permit the licensee or registrant to resume the servicing of mortgage loans subject to any terms, conditions, and limitations the Commissioner prescribed, if he or she were satisfied that termination could be done safely and was in the public interest.

#### Other Provisions

The bill specifies that all fees received under the bill would have to be deposited in the State Treasury and placed in a special fund. The fund would be administered by the Commissioner. Money placed in the fund would have to be directed to the operation of the FIB.

Also, all compensation and expenses required to be reimbursed to the FIB in connection with a conservatorship would have to be deposited in the State Treasury and directed to a bureau revolving fund. Money in the fund and interest earned could be disbursed only on proper vouchers, approved by the Commissioner, to reimburse the FIB for expenses incurred in connection with conservators of licensees and registrants.

The bill would permit a licensee or registrant to require a borrower to pay "reasonable and necessary" charges reflecting actual expenses incurred in connection with the making, closing, disbursing, extending, readjusting, or renewing of a mortgage loan. The charges would be in addition to interest authorized by law and would not be a part of the interest collected or agreed to be paid on the loan. "Reasonable and necessary" charges would consist of fees for recording, title examination, title insurance, the preparation of a deed, appraisal, or credit report, and loan processing. Charges could be paid only once by the borrower to the licensee or registrant.

Under the bill, a mortgage servicer would have to deliver an annual statement to the borrower detailing the borrower's account and showing the unpaid balance of the loan at the end of the preceding 12-month period, interest paid during that period, and amounts deposited into escrow and disbursed from escrow during that period. Within 25 days of receiving a written request from the borrower, a mortgage servicer would have to deliver to the borrower a ledger history of the borrower's account showing the date and amount of all payments made or credited to the account. The servicer would not have to furnish more than one annual statement and one ledger history in any 12-month period. A fee could not be charged for the annual statement or for one ledger history in a 12-month period.

The bill states that, if the real property is located in Michigan, a mortgage loan would be subject to the proposed Act and other applicable laws of this State, regardless of the place of execution of a mortgage loan. In addition, failure to comply with the provisions of the bill would not affect the validity or enforceability of any mortgage loan, unless the loan were invalid or unenforceable under other State or Federal laws.

#### House Bill 4702 (S-1)

House Bill 4702 (S-1) would amend the Occupational Code to excuse from regulation as a real estate broker, associate broker, or sales person, someone who was regulated under the "Mortgage Brokers, Lenders, and Servicers Licensing Act", proposed under House Bill 4701 (S-3), and who did not perform other acts requiring licensure under the Code.

MCL 339.2503

#### House Bill 4703 (S-1)

House Bill 4703 (S-1) would amend the Uniform Securities Act to exempt from registration as a broker-dealer, for the purchase or sale of mortgage loans, someone who was licensed or registered under the "Mortgage Brokers, Lenders, and Servicers Licensing Act" proposed under House Bill 4701 (S-3).

MCL 451.601

### **SENATE COMMITTEE ACTION**

The Senate Committee on Commerce and Technology substitute (S-3) to the Senate Bill 4701 that would require an applicant for licensure who acted solely as a mortgage broker and received funds from a prospective borrower prior to the mortgage closing to deposit \$25,000 as proof of financial responsibility and to meet minimum net worth requirements. The House-passed version of the bill would impose those requirements on all applicants who acted solely as mortgage brokers. In addition, the substitute would permit the Commissioner to reduce, waive, or modify the requirements for proof of financial responsibility for small operators who serviced no more than 300 mortgages or land contracts and did not collect money for payment of taxes or insurance on those mortgages or contracts.

The substitute also includes a provision to permit Michigan's six current "Class R" broker-dealers to retain their affiliations with mortgage dealers. (The bill generally would prohibit such affiliations.) Under the substitute, a broker-dealer who acquired a license prior to September 1, 1987, and had maintained that license continuously subsequent to that date, could continue to operate legally as an affiliated broker-dealer.

Finally, the House-passed version would exempt agencies of the United States and of Michigan from the bill's license and registration provisions. The substitute would include "corporate instrumentalities" of the United States and of Michigan within that exemption.

The Senate Committee adopted a substitute (S-1) to House bill 4702 that merely incorporated language that had been added to the affected section (MCL 339.2503) by Public

Act 63 of 1987. The Senate Committee also adopted a substitute (S-1) to House bill 4703 that specifies that the exemption from registration under the Uniform Securities Act would be "for the purchase or sale of mortgage loans as defined" in House Bill 4701 (S-3). The House-passed version would apply the exemption "for activities regulated under" House Bill 4701.

### **FISCAL IMPACT**

Based on the number of licensees per capita in other states which license mortgage brokers, the FIB is expecting about 700 applications for licenses or registration under the bills — the majority of which would be for licenses.

If, therefore, 75% of the initial applications were for licenses (525) and 25% were for registration (175), the FIB would receive the following revenue from licensing and registration fees:

1st Year	Total: \$315,000		Subsequent Years Total: \$210,000	
Fees	525 Licensees	175 Registrants	525 Licensees	175 Registrants
\$200 inspection fee	\$105,000	0	0	0
\$300 license/renewal	157,500	0	\$157,500	0
\$300 registration/renewal	0	52,500	0	52,500
<b>TOTAL</b>	<b>\$262,500</b>	<b>52,500</b>	<b>\$157,500</b>	<b>52,500</b>

In addition, the FIB would be required to charge licensees and registrants for the costs of examinations and inspections conducted under the bills, including an hourly rate of between \$20 and \$40 for each examiner, the cost of independent investigators, and actual and reasonable travel, lodging, and meal expenses for examiners traveling out of State.

The FBI states that it would need 15 FTEs (1 secretary, 1 clerk and 13 examiners) and \$750,000/yr. to operate the program. Assuming that the FTE positions would be new and the following standard administrative costs applicable —

— Typist Clerk III		
(\$10.14/hr. x 2,088 hrs.) + 37.5% (\$10.14 x 2,088)	=	\$29,112*
— Secretary IV		
(\$10.72/hr. x 2,088 hrs.) + 37.5% (\$10.72 x 2,088)	=	30,777
— Modular Workstations — 2 x \$1,800	=	3,600
— Rent/Office Space		
(2 x 150 sq. ft./person) x \$11.50 sq. ft./year	=	3,450
— Phones = 2 x \$100/phone	=	200
		<b>\$67,139</b>

\* (annual salary and fringe benefits (37.5% of annual salary))

it would appear that most of the program's implementation and operational costs could be attributed to the examiners. Since the examiners generally operate from their homes, the only expenses they would incur would be for travel, lodging, meals and time spent actually examining or investigating licensees or registrants — expenses which the bills already specify would have to be paid by the licensees and registrants. It would appear, therefore, that the licensing, registration and inspection/examination fees provided in the bills would eventually be sufficient to fund the program. It is likely, however, the FBI would need GF/GP funds to cover start up costs, including the costs of educating the public about the new licensing and registration requirements, since there would be a delay between implementation of the program and initial collection of the fees.

#### **House Bill 4702 (S-1)**

The bill could result in an indeterminate revenue loss to the State's GF/GP fund if real estate brokers and salespersons licensed under the Occupational Code were to be licensed under House Bill 4701 (S-3), since their license fees would then be deposited in a restricted fund for use by the Financial Institutions Bureau. Currently, real estate license fees lapse to the General Fund.

#### **House Bill 4703 (S-1)**

The bill could result in an indeterminate revenue loss to the State's GF/GP fund if broker-dealers licensed under the Uniform Securities Act were to be licensed under House Bill 4701 (S-3), since their license fees would then be deposited in a restricted fund for use by the Financial Institutions Bureau. Currently, broker-dealer fees lapse to the General Fund.



## ARGUMENTS

### Supporting Argument

The bills would enact reasonable, effective regulation of first mortgage lenders, servicers, and brokers who otherwise are not regulated under comprehensive regulatory acts. After the 1980 Federal deregulation of first mortgage interest rates and fees, abuses in the mortgage industry (which tended to be in the form of exorbitant fees imposed in order to avoid State interest rate ceilings) could no longer be combatted by application of State usury laws. After the 1981 enactment of the State's secondary mortgage loan Act (MCL 493.51-493.81), abuses became more apparent in the first mortgages business. Such abuses culminated with the allegation that Diamond Mortgage was assigning mortgages to more than one investor, charging astronomical fees, and failing to disburse funds to borrowers.

Some State officials contend that these abuses went undetected because of fragmentary authority: the Attorney General can seek injunctive relief under the Consumer Protection Act for unfair or deceptive practices; the Commerce Department's Corporations and Securities Bureau has authority to enforce securities laws; the Department of Licensing and Regulation oversees regulation of real estate brokers who arrange mortgages; and the Financial Institutions Bureau monitors the activities of lenders regulated under various comprehensive laws (e.g., the Banking Code and the Credit Union Act) and the secondary mortgage Act. No one agency, however, has the responsibility or the authority to monitor and regulate the first mortgage industry. While A.J. Obie was registered as a securities broker-dealer and was under the jurisdiction of the Corporations and Securities Bureau, State officials claim they had no authority to examine and monitor Diamond Mortgage. The bills would fill that regulatory gap, without imposing dual regulation upon those who are already adequately regulated. Also, House Bill 4701 (S-3) would include provisions to sustain the livelihood of some operators (e.g., small-scale mortgage servicers and Class R broker-dealers) that otherwise would be put of business by the bill. The problem is by no means in the past. Given the Federal tax law reforms, interest paid on first mortgages and home equity loans are among the few deductions remaining available to many; consequently, the potential for abuse in the industry is as great as ever.

### Opposing Argument

Some have challenged the need for the bills. The State already has a number of laws under which first mortgage transactions can be regulated. The Consumer Protection Act provides a broad range of authority to obtain relief from unfair practices. Those who negotiate mortgage loans are subject to the Occupational Code's regulation of real estate brokers, with its license and bonding requirements and various remedies. The buying and selling of mortgage loans is subject to the Uniform Securities Act's provisions for regulation of broker-dealers. Finally, there are laws against fraudulent activities. Diamond Mortgage acted as a real estate broker, and A.J. Obie was a securities broker. Many suspect that the problem was not a lack of regulatory authority, but a lack of enforcement. What use would be served by a new licensing Act if current regulatory laws are not enforced adequately?

**Response:** Since the activities of Diamond Mortgage and A.J. Obie stretched across the regulatory purview of various departments and agencies, the companies were able to operate a complex deceptive scheme without detection. The problem was an absence of any centralized or coordinated regulatory capability. House Bill 4701 (S-3) would provide the framework for effective, concentrated regulation of mortgage brokers, lenders, and servicers.

### Opposing Argument

House Bill 4701 (S-3) should go further to protect consumers. Mortgage loan abuses largely have been in the form of excessive fees, and the bill would not do enough to forbid them. The bill should expressly override (as States are permitted to do) the Federal preemption of limits on loan discount points and set specific limits on the size of the loan processing fee, which arguably represents discount points. In addition, the bill should make consumer access to accounts easier. A person should be able to obtain a complete ledger history, not just one for the previous twelve months. There is a need to protect individual mortgages. House Bill 4701 (S-3) provides that failure to comply would not affect the validity or enforceability of any mortgage loan not rendered invalid by another law. Would this mean that a mortgage could be foreclosed even though, for example, funds had not been disbursed to borrowers? The bill should establish claims and defenses for borrowers.

The bill also fails to address adequately the problem of mortgage lenders reneging on promises of certain interest rates. It would be a violation of the bill to fail to make a mortgage loan in accordance with a written agreement, but that does not go far enough. The problem has more to do with loopholes written into agreements. At times, some lenders have promised to preserve a given interest rate for a certain period of time, then, as rates rose, delayed action on the mortgage application until the specified time period had expired.

**Response:** The bill would protect consumers adequately. Under the bill's standards, fees would have to represent reasonable and necessary costs. The specific fees listed by the bill would not be subject to Federal preemption, except perhaps for the loan processing fee, which, along with other fees, would be monitored closely by the Financial Institutions Bureau for reasonableness. Should abuses recur, the law could be modified appropriately. The key to the bill is its strong monitoring capability that would enable discovery of problems before they reached disastrous proportions, along with provisions that would help to ensure that new licensees were reputable. Stiffer restrictions such as increased bonding or net worth requirements would serve only to limit competition and entry into the industry. Further, the penalties that would attach to what the bill calls "misdemeanors" actually would be more in line with felony penalties. Finally, borrowers would be protected through provisions for restitution and other equitable remedies, and a requirement that at least 75% of a mortgage's proceeds be disbursed to the borrower before the mortgage could be sold on the secondary market.

Legislative Analyst: P. Affholter  
Fiscal Analyst: L. Burghardt

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