Ethics and Consumer Protection

IV. G. Ethical behavior
1. Consumers
2. Appraisers
3. Underwriters
4. Investors
5. Warehouse lenders
6. Real estate licensees
7. Closing agents
8. Employers

Overview

This lesson discusses ethical practices and consumer protection responsibilities of a mortgage broker and loan originator.

Objectives

At the conclusion of this lesson, the student will be able to:
1. Describe features of predatory lending.
2. Identify significant challenges to ethical behavior in mortgage lending.
3. Explain a mortgage licensee’s ethical duties in relation to sales and marketing.
4. Explain the responsibilities of a mortgage licensee in terms of suitability.
5. Identify areas of ethical responsibility in the processing of a loan application.

Ethics

----- WHY TALK ABOUT ETHICS -----

In any mortgage loan transaction, there is a potential for either the borrower or the lender to suffer a loss. The risk to the borrower is that he may pay excessive loan fees or that he may not get a loan suitable to his needs, exposing him to the risk of default, foreclosure, and the loss of his home. The risk to the lender is the loss of capital invested in the loan. Because residential mortgage loans are secured by real property, the risk to the lender or investor is lower than the risk for other types of loans. However, a lender can suffer losses if the borrower defaults, requiring the lender to foreclose on the property; files bankruptcy; or refinances the loan at a lower rate, reducing the return the lender had projected. Unlike the borrower or the lender, a mortgage broker and loan originator have no longterm interest in the performance of a loan. If they fail to match the borrower with the proper loan or fail to provide accurate information for
underwriting, there will be an increased probability that the borrower will default. This will adversely affect the lender or the eventual purchaser of the loan and will create dire consequences for the borrower. However, depending on the terms of his mortgage broker agreement, the mortgage broker and loan originator may avoid adverse effects. Today many mortgage broker agreements have clauses that do create consequences for a mortgage broker who engages in improper acts in originating a loan. These clauses may obligate the broker to indemnify the lender against losses, and return all benefits (i.e., fees, commissions, etc.) received, arising out of:

- acts or omissions of the broker or persons representing the broker, including any misrepresentation or fraud in the origination, processing, closing and funding of a mortgage loan;
- early default by the borrower or some other event triggering a repurchase obligation, including a material misrepresentation in which the broker or its loan originator participated;
- demand by an investor to indemnify or make the investor whole with respect to a mortgage loan;
- repayment of the loan within the first six months after the recording date.

What’s the Problem?

Because the broker is compensated for originating a loan as long as the lender accepts it, and may not be penalized if he does not actually commit any misrepresentation and the borrower defaults later in the term of the loan, he will have less concern with the suitability of the loan for the borrower or with the accuracy of information presented in the mortgage application than the lender. His primary concern is to provide enough information so the mortgage lender will fund the loan and pay his fees. This creates a conflict between his opportunity for personal financial gain and the proper performance of his responsibilities.

The relative lack of consequences for a lender’s agent subjects the mortgage delivery system to what economists and political scientists call the principal-agent problem. Evidence of this problem has been produced in studies showing that borrowers of loans originated by brokers:

- are more likely to prepay faster and to default than similar borrowers who obtained loans through retail sources.
- are charged a higher interest rate in order to compensate the lenders for the higher risk of default and prepayment created by the principal-agent problem.

Among the brokerage practices decried by consumer advocates are the following:

- Marketing higher than market-rate loans in low-income neighborhoods
- Convincing elderly homeowners to refinance homes that have a low mortgage balance
- Locking consumers into high interest rate loans with substantial prepayment penalties
- Convincing borrowers to borrow more than they can afford by utilizing creative loan packages, including negative amortization or loans with large balloon payments
- Loan flipping
- Lending without regard for the ability to repay

And then there’s…
Predatory Lending

A number of actions of lenders and their loan originators have earned the term “predatory lending.” Most regulators consider predatory lending to be the extension of credit to borrowers who cannot afford the credit on the terms being offered. Predatory loans can be recognized by one or more of the following features designed to “strip away” or reduce a borrower’s equity in the collateral and increase the likelihood of foreclosure:

- **Targeting**: Predatory lenders and mortgage brokers target persons with limited access to mainstream sources of credit (e.g., the elderly, poor or uneducated borrowers) who are vulnerable to abusive practices, and use fraudulent, deceptive, or high-pressure sales tactics to get them to accept loans that are not affordable or in their best interest. They will inadequately disclose the true costs, risks and appropriateness of the transaction to the borrower. Often they will use bait-and-switch tactics, knowingly advertising or offering one set of terms which are more appealing but are not readily available and then pressuring the borrower into signing a contract with more expensive terms and hidden fees.

- **Steering**: Steering is the practice of directing a borrower toward a subprime loan when he could qualify for a more standard loan. It is estimated that almost 50% of subprime borrowers could have qualified for loans with lower fees and rates. Steering can also refer to directing borrowers to settlement service providers with whom the broker or lender has a relationship, either because of financial benefit to the broker or lender or because that service provider will help bend rules to get a loan approved.

- **Lending without regard to repayment ability (asset-based lending)**: Typically, the predatory lender will make the loan based on the borrower’s home equity and the foreclosure value of the collateral, rather than on a determination that the borrower can make the payments as scheduled in the loan terms and based on the borrower’s current and expected income, current obligations, employment status, and other relevant financial resources. The lender simply relies on its ability to seize the borrower’s equity in the collateral to satisfy the debt and to recover the high fees associated with the loan. The result is higher-than-normal foreclosure rates. Foreclosure enables the lender to acquire the borrower’s property and equity through the foreclosure sale.

- **Packing**: Packing is the inclusion in the loan principal amount of such costs as points, mortgage broker fees, prepayment penalties on a prior loan, and charges for additional related products, such as single-premium credit life insurance, without the borrower’s informed consent. Because packing enables a borrower to pay expenses over time, instead of at closing, it is an attractive way to add costs, which may be unnecessary or excessive, to the loan. In the case of credit life insurance, informed consent would involve explaining the purpose of the insurance, the fact that it could be obtained elsewhere or that other insurance could cover the same risk, and the fact that it is not required for loan approval. Because it may be sold by a person with a license limited to the sale of such insurance, informed consent is often not provided. Credit life insurance provides for repayment of the loan should the borrower die. Because the borrower does not have to prove insurability, it is more expensive than insurance purchased separately. While it may be useful when paid for on a monthly basis, when it is sold as a single-premium policy, which is paid for up front, the borrower usually cannot afford to pay the
premium in cash and must finance it. This makes the loan even more expensive and strips equity from the borrower. Fannie Mae and Freddie Mac will not buy any loan that includes financed credit insurance.

- **Excessive rates and fees**: While risk-based pricing may justify higher rates and fees, charging excessive rates to a borrower who qualifies for lower rates and/or fees offered by the lender is considered predatory behavior. While the typical loan may have up-front fees around 1% of the loan amount, predatory loans often have fees in excess of 5% of the loan amount even though such fees do not have anything to do with the credit risk of the borrower. As with packed costs, these fees are financed into the loan, decreasing the homeowner’s equity. In addition to the excessive fees, the interest rate may be extremely high. While a high interest rate may be justified based on risk-based pricing, predatory loans would have rates in excess of those that would be justified by the risk of default. Such loans often impose excessive rates on borrowers who would present minimal or nonexistent risk simply because they have been marketed to persons who are not aware of their borrowing opportunities.

- **Padding costs**: Predatory lenders may pad costs:
  - by charging borrowers for a detailed appraisal when only a drive-by appraisal was done.
  - by charging the borrower recording fees and other fees, such as document preparation fees or credit report fees, many times the actual cost.
  - by charging broker fees when the borrower never met or knew of the broker.
  - by itemizing charges that are duplicative or should be included under other charges, (e.g., charging a loan origination fee plus separate, additional charges for underwriting and loan preparation).

- **Flipping**: Flipping is repeated refinancing of a loan within a short period of time, without any real benefit to the borrower. The primary objective of the mortgage broker and/or lender is to generate additional loan points, loan fees, prepayment penalties, and fees from financing the sale of credit-related products. In some cases, lenders will originate balloon or adjustable-rate mortgages and then inform the borrowers of this fact after closing so they will apply for a new fixed-rate loan to pay off the entire balance. In other cases, lenders will purposely structure the loan so the payments are unaffordable. Then when the borrower has to return to the lender to refinance the loan in order to avoid foreclosure, he is charged additional points and fees. Typically, the new loan is just as unaffordable as the first, and the result is still foreclosure.

**For Example**

After living in her home for 42 years, 81-year-old Mrs. P decided to remodel her home, which at the time was paid for. When the contractor she hired went bankrupt before completing the project, she refinanced her home with an adjustable-rate mortgage through a subprime lender to pay a second contractor to complete the work. Various brokers convinced her to refinance an additional three times over the next four years. Each time she refinanced, the loan balance increased until she had an outstanding mortgage balance of $117,000 and monthly payments of $911, not including taxes and insurance. This is a classic case of loan flipping.

- **Prepayment penalties**: Prepayment penalties are charges for early payoff of the loan. They serve as deferred fees that the lender expects to receive and the borrower never expects to pay. While only 2% of borrowers have prepayment penalties with loans obtained in the conventional market, as many as 80% of the borrowers in the subprime
market have such penalties, often imposed for more than three years. Statistics show that more than half of subprime borrowers are forced to prepay their loans with penalties. Prepayment penalties serve to discourage a borrower from refinancing to obtain a loan at a lower interest rate when his credit improves to the point where he can move out of the subprime market or to simply obtain an affordable loan. The penalty may keep a borrower with temporary credit problems trapped in the high-rate loan in order to avoid paying the high fee, which is often as much as six months’ interest or 5% of the loan balance. If a borrower does prepay, the penalty will strip his equity. As a result of the problems caused by prepayment penalties, the Truth-in-Lending Act and Regulation Z have placed the following restrictions on prepayment penalties in loans subject to HOEPA regulation and on other higher-priced mortgage loans:

- The penalty cannot apply:
  - beyond two years after loan consummation;
  - if another loan from the same creditor is refinancing the loan.
- The amount of the periodic payment of principal and/or interest may not change during the four-year period following consummation.
- For a HOEPA-regulated loan, there can be no prepayment penalty if the consumer’s total monthly debt payments exceed 50% of his monthly gross income at the consummation of the loan.

- **Loan terms**: Some loan terms (e.g., negative amortization) make it more difficult or impossible for borrowers to reduce or repay their indebtedness. With negative amortization, the monthly payment does not pay off all the accrued interest, so the principal balance will increase each month. The borrower may end up owing more than the amount originally borrowed and have to make a balloon payment at the end of the loan term.

- **Balloon payments**: These payments conceal the true burden of the financing and force borrowers into refinancing transactions or foreclosures. When a loan is structured so that the payments apply primarily to interest, most or all of the amount borrowed will be owed upon maturity of the loan. A borrower who cannot afford the balloon payment will either lose the home through foreclosure or be forced to refinance with the same or another lender for an additional term at additional cost. Now under Regulation Z, except for a bridge loan with a term of less than one year, a loan subject to HOEPA with a term of less than five years cannot have a payment schedule with regular payments, that when totaled, do not fully amortize the loan.

- **Mandatory arbitration clauses**: Predispute mandatory binding arbitration clauses prevent effective review of unfair and deceptive practices and prevent consumers from obtaining injunctive relief against wrongful practices, proceeding on behalf of a class, or obtaining punitive damages. To go through arbitration, the borrower may have to pay costly fees, travel to a distant location, accept a prolender arbitrator, and spend time he may not have when facing foreclosure. A fairer practice would be to allow an informed borrower to voluntarily agree to arbitration if and when he considers it helpful in resolving a dispute with a lender.

----- **THE CALL TO ACTION** -----

There have been calls on legislators at both the state and federal level to control predatory lending and place stronger regulation on the mortgage lending industry. All states are adopting
licensing and educational requirements for mortgage brokers and loan originators. In addition, there is a push to develop and promote an industrywide standard for ethical behavior. Many companies in the industry are adopting a companywide code of conduct for their employees to follow.

What’s the Legal Thing to Do?

A mortgage professional must comply with various state and federal statutes and regulations relating to the conduct of his business. Laws and regulations define the minimum type and level of professional conduct that practitioners may use without penalty from society. As a result, legal rules established by law and administrative regulations are by and large clear. For example, unfair lending practices laws forbid, among other things:

- discrimination in lending.
- inconsistencies in credit evaluation and reporting.
- failure to disclose fully all terms and conditions of financing.
- incomplete itemization of all projected and/or actual costs associated with settlement.
- undisclosed business relationships with parties to the transaction.
- misrepresentation in advertising.
- improperly maintaining documentation in the loan file. A violator can be ordered to cease and desist, fined, or have his license suspended or revoked. Penalties are subject to judicial review.

Statutes and Regulations

The minimum level of legal and ethical responsibility is compliance with statutes and administrative regulations. A mortgage broker must comply with numerous federal laws, including the following:

- The Equal Credit Opportunity Act (ECOA) and Regulation B, which prohibit discrimination against loan applicants based on race, color, religion, national origin, sex, marital status or age
- The Fair Credit Reporting Act (FCRA), which establishes requirements for credit reporting and credit worthiness of applicants
- The Fair Housing Act, which prohibits discrimination in the sale, rental, and financing of any residential housing based on race, color, religion, national origin, sex, familial status or mental or physical handicap
- The Home Mortgage Disclosure Act (HMDA) and Regulation C, which require that specific information be made available to the public when mortgages are sold on the secondary market
- The Home Ownership and Equity Protection Act (HOEPA), which requires specific disclosures on loans with APRs more than eight percentage points on first liens and more than ten percentage points on subsequent liens, above the rates on United States Treasury Securities of comparable maturity
- The Real Estate Settlement Procedures Act (RESPA) and Regulation X, which require the disclosure of fees and costs involved when closing home mortgages and prohibit abusive settlement practices, including payment of anything of value for a referral. (The way to generate referrals should be open communication with any referrer during the loan
process and appreciation shown in words and by proper handling of the needs of the person referred).

- The Truth in Lending Act (TILA) and Regulation Z, which require disclosure of loan terms and percentage rates in a form that makes it easier for a consumer to compare loans

What’s the Ethical Thing to Do?

Ethics goes beyond what is required under the law, so ethical rules will extend beyond the minimum legal standards in providing guidance for one’s actions. Ethics goes into the realm of what should be done. As a result, ethical rules are often not as clear-cut as the legal rules.

A current topic of debate is what, if any, fiduciary responsibilities does a mortgage broker or loan originator owe to a borrower. Fiduciary responsibilities are those of loyalty and trust owed by a person who holds funds in trust for another or by a person acting as an agent of another. There is no dispute that a mortgage broker holding funds deposited by an applicant has a duty to safeguard those funds and not misuse them. Disputes arise when deciding whether the broker represents a lender, himself or an applicant. In some states, a mortgage broker may be considered an agent of the applicant or borrower, and therefore, is obligated to provide him with a loan that is suitable. Providing a loan that is not, creates liability for the broker. Elsewhere, the prevailing attitude may still be caveat emptor (buyer beware). This holds that the buyer is responsible for using due diligence to determine whether his purchase is beneficial or suitable.

A mortgage broker should ensure he is working with good lenders by becoming acquainted with them. As with most relationships, the way to determine quality is to work with them over a period of time and judge them by their performance.

Ethical Challenges

The following are probably the greatest challenges to ethical behavior facing those in the mortgage lending business:

- A personal need to achieve success and the financial pressures to provide security for family or others
- Factors related to competition in the industry, and in business in general, that may lead to a company environment/culture that encourages a professional to compromise his ethical values in order to achieve organizational goals: make the sale “at all costs”
- Managers and performance standards, such as quotas, that may pressure loan originators to produce regardless of the methods used to achieve desired results
- Methods of compensation, such as commissions, yield-spread premiums, bonuses, or opportunities for profit-sharing, that encourage sales over service
- Lack of company support for ethical behavior, as evidenced by the lack of a company ethics policy, a lack of communication of a company ethics policy, or a lack of ethics training by the company (Failure to assertively promote an ethics policy will increase the likelihood of unethical behavior, unethical demands made by coworkers, and fear of management reprisal for disclosure of unethical activity.)
- General confusion among borrowers about how interest rates and points interact (The borrower may overlook higher points and costs added into the loan amount by looking
only at the “low rate” or failing to anticipate the consequences of the lapse of an introductory rate.)

- Unethical demands made by borrowers (Limited doc or no doc applications encourage applicants to exaggerate or fabricate income, employment or asset information. While the loan originator may earn a fee for processing the application, there is a strong possibility that a loan obtained in such a manner will eventually become a major problem for the borrower, who cannot afford it, and for the lender or eventual investor, who must deal with a default and foreclosure.) A mortgage broker has ethical responsibilities to both the borrower and the lender throughout the loan process to try to minimize their exposure to these risks. Whether obligated by statute or not, a mortgage broker’s function should be to match a borrower with a suitable loan product. A broker performing at a high level of ethical responsibility will attempt to match the borrower with the best product for him. In a conflict of interest situation, the broker must place the interests of the client first. A loan originator or broker has a responsibility to the borrower and the lender to be honest and adequately disclose all material facts and to ensure all agreements are in writing.

For Example

A lender has an agreement with Mel Lowe to give qualified borrowers a certain interest rate. Mel then tells Ivana Lone, a qualified borrower, that the rate is locked in with the lender, but Ivana is not asked by Mel or the lender to sign a lock-in agreement. The lender then informs Mel it will not honor its agreement with Mel to provide the interest rate. Thus, Mel cannot offer Ivana a loan at the promised rate and Ivana has no written agreement to enforce against the lender.

For Example

After mortgage broker Mel Lowe informs Anita Lone that she lacks sufficient income to qualify for the loan she wants, Anita suddenly recalls that she makes double her previously stated income, based upon her side business. She later provides Mel with documents supporting the additional income. Mel, although suspicious, does not question Anita about the additional income and submits an application that includes it. After the loan closes, the lender discovers the claimed additional income never existed. A loan originator or broker is also expected to be knowledgeable and professional, deal in good faith and exercise reasonable care, skill and diligence on a customer’s and lender’s behalf. This includes using due diligence to be alert to fraud, avoiding providing advice beyond his scope of expertise (e.g., advice regarding tax consequences of any action relating to financing) and monitoring the progress of a loan through to underwriting.

For Example

Sally Forth, a loan processor at Gofer Brokers, quit the firm after just taking a number of borrower applications. Gofer failed to follow up on Sally’s application files. A borrower assumed that Gofer was processing his loan, until he contacted the mortgage broker as his closing date approached. Gofer immediately sent in the borrowers’ information to the lender. The lender determined that the borrowers did not qualify for the loans promised by the mortgage broker. The borrower’s purchase transaction deadline expired, and the seller decided to accept a better backup offer on his property.

Consumer Protection
A broker’s ethical responsibilities begin with his sales and marketing efforts and his cultivation of referral sources in order to obtain business.

The number one ethical problem cited in surveys of professionals and managers is false or misleading representation of products or services in marketing, advertising or sales efforts, usually involving various aspects of loan terms. This includes:

- use of false or misleading advertising.
- use of truthful advertising in a deceptive or misleading manner.
- concealing the limitations of the programs or terms being promoted.

Most states have laws prohibiting false advertising used to promote loan programs, whether:

- on TV, radio or the Internet.
- in print in descriptive literature, brochures, sales illustrations or sales aids.
- in slide shows or prepared group talks.

The purpose of these laws is to help ensure that loan products are promoted accurately, without exaggeration of their benefits or minimization of their drawbacks. While there may be conflicting opinions as to what is considered false advertising, ethical practice would be to make sure that any advertising used cannot be easily misinterpreted and that it is not intended to mislead either by direct statement or by concealment of facts that need to be revealed in order to avoid misinterpretation of statements that were made. Ads that tout low monthly payments or low interest rates must include adequate disclosure of other terms, such as the fact that the stated rate will apply only during a loan’s initial period, that payments will increase and there may be a final balloon payment required. A mortgage broker must avoid bait-and-switch tactics: knowingly advertising or offering one set of terms which are more appealing but are not readily available and then pressuring the borrower into signing a contract with more expensive terms and hidden fees. Of course, compensation for referrals is not only unethical but a violation of RESPA. Referrals should be earned by performance. Having to pay for referrals is an indication that the service being provided is not good enough to merit the referral on its own.

The results of presenting borrowers with disclosures and expecting them to arrive at beneficial decisions have been somewhat disastrous. Therefore, today a loan originator must realize that he does have some responsibility, even if not required by statutes, to ensure that he is providing loan programs that are suitable for an applicant. He has a duty to provide advice and service which are in the applicant’s best interest. In order to do so, he must make a conscientious effort to ascertain and to understand all relevant circumstances surrounding the client. Before attempting to take a complete loan application, he should:

- evaluate the applicant’s qualifications.
- identify the applicant’s personal and financial objectives.
- align loan programs with the applicant’s circumstances.
- perform financial and homeownership counseling, where applicable.
To provide ethical customer service, the mortgage broker must carefully assess the applicant’s needs, educate him about financing alternatives, help solve problems that arise in the loan approval process, and be an advocate for the applicant. The loan originator should not assume he knows what a potential borrower wants or needs. Instead, the loan originator should assess the applicant’s needs, determine his use of the funds and explore options that might best satisfy those needs. As each borrower’s circumstances are just a bit different, the loan originator should listen and respond to a borrower’s questions as if he has never heard them asked before. A major ethical problem in the mortgage industry is the failure to identify a customer’s needs so as to be able to recommend products and services to meet those needs. Instead, oftentimes, a recommendation is made so the loan originator can make a fee or a higher fee. The loan originator should recommend only loan programs suiting the needs of the applicant. The transaction should have a reasonable, tangible net benefit to the borrower, taking into account the terms and costs of the loan as well as the borrower’s circumstances (e.g., the borrower’s objectives in obtaining the loan, his credit history and ability to pay, as measured by his debt-to-income ratio, his employment and his financial resources). This means the loan originator must make a reasonable inquiry concerning the borrower’s current and prospective income, existing debts and other obligations, and any other information the loan originator should know and then exert his best efforts to recommend, seek out or originate a loan that takes that information into consideration. Many of the problems arising from subprime lending are the result of mortgage brokers who convinced borrowers that they should apply for loans for which they could qualify based only on initial loan terms, which included interest-only payments, low initial ARM interest rates, or low fixed rates for a limited period. However, when the initial terms were scheduled to change, the only way for the borrower to deal with the loan would be to refinance it or to sell the property. This thinking was based on a presumption that an unprecedented period of real property appreciation would continue. The needs of a borrower who intended to remain in his home for a number of years would probably have been better served by purchasing a more affordable property for which he would not have to depend upon a qualification process that, by its very nature, indicated he could not afford the eventual payments.

Other problems relating to subprime lending arose from the decision to relax underwriting standards to allow borrowers to qualify without having to verify income, assets, or anything else. Instead of merely making it easier to obtain speedy loan approval, it became easier to falsify data. Unethical mortgage brokers, who had nothing to lose processing loans that would default in two years (and after the broker received his nonrefundable brokerage fees) might not merely encourage applications that were suspect, but might encourage borrowers to falsify information in order to obtain their loan or to obtain a loan on a more expensive property. This activity would harm not only the lender or investor holding the loan at the time of default, but the borrower who would lose his home, and the community in which the foreclosed home was located as well. Promotion of refinancing can present ethical problems. Similar to boiler room telemarketing fraud, an unscrupulous broker may target people who have recently refinanced with a subprime lender to refinance again by convincing the borrower that he can get them a better interest rate and some cash back. Ethical practice would include careful calculations to determine the cost-effectiveness of refinancing. Time horizons, money cost, and the impact of increased indebtedness for the borrower would be considered in order to determine whether a new loan would be truly beneficial. To help make this determination, the originator or broker must become
familiar with the terms and conditions of the existing loan and any factors that would cause the borrower to want to retain that loan (e.g., fixed rate, adjustable terms, current amount of monthly payments going to principal reduction, loan balance, etc.).

While it may be tempting to simply agree with a borrower who has decided he wishes to refinance, in order to earn the fees, the loan originator should only promote the refinance when he is sure the borrower:

• understands all costs and negative aspects.
• is able to evaluate fully the implications of the new loan.
• still believes the refinance is the best course of action.

----- PROCESSING ----- 

Once he has identified the proper loan program for a borrower, the loan originator will:

• complete the application and gather required documentation.
• make all regulatory and informational disclosures in good faith.
• communicate with the applicant throughout the loan process to make sure he is aware of the loan status and resolve any problems.
• obtain a loan commitment and satisfy any underwriting conditions.
• inform the applicant of any adverse action and his rights in relation to such action.

Disclosures 

The loan originator will provide a good faith estimate and other disclosures at the time of loan application. All disclosures must be given or mailed to the borrower within three business days of the application. The borrower should understand that some fees are negotiable and that he is free to shop around or he may pay more for brokerage services than necessary.

Regulation Z requires that the following statement be included in the TILA disclosures, “You are not required to complete this agreement merely because you have received these disclosures or signed a loan application.” RESPA and the Truth in Lending Act require the good faith estimate and the TILA disclosures to be updated if figures change. The borrower must be informed of any major changes in fees or the interest rate from the time of the estimate as such changes can have a significant negative impact on him. If he is not made aware of the changes prior to closing, he is free to refuse the offered loan. However, he may be reluctant to do so because:

• he will lose all up-front fees paid in the loan process.
• he may have to forfeit his earnest money deposit for failing to close by the specified closing.
• if he has already closed on the sale of his current home, he may need to take the loan to make sure his family has a place to live.

Communication 

Communication is vital to processing, and lack of communication with the borrower can result in lost business. It is very important to keep the borrower aware of the status of his file. If there is a
change in the file that has an adverse effect on the borrower, an adverse action form must be sent to the borrower.

Mortgage lending rules, regulations, disclosures, and practices can seem very intimidating and confusing to many potential borrowers. The loan originator needs to be able to explain the process simply, concisely and without the use of jargon; he must avoid unnecessary details and focus on what matters to the customer. He should explain briefly how the loan process will work and explain the need for and process of obtaining documentation, such as bank statements, tax returns, pay stubs, divorce papers and verifications of employment and deposits. The borrower should also be reminded that:

- there are no guarantees of approval.
- additional documentation may be required.
- the expected date of closing in the sales agreement is really no more than a target date.

Use of examples, stories, illustrations and past experiences in helping customers can avoid and solve common problems and help build credibility and establish rapport. They can also help unearth items in the borrower’s past in time to prevent problems in processing and underwriting.

A loan originator’s actions must be fair. He can project the image of fairness by using such words as “Everyone needs to provide two copies of their…” or “Everyone needs to bring all of the items on the enclosed checklist,” instead of “You need to …” A “checklist mentality” will help the loan originator address documentation needs, manage disclosure requirements, follow-up and closing, and provide “ticklers” that will keep the processing moving smoothly.

Throughout the process, the loan originator should make sure that the borrower:

- understands what is taking or has taken place.
- knows whom to contact if he has questions later.
- feels comfortable contacting that person. Calling the customer after a loan application interview to ask if he has any questions or concerns can build strong customer loyalty.

As perception is important, the loan originator needs to ensure that the borrower knows that the loan originator is on his side and will advocate strongly for his loan application. While the loan originator cannot promise a loan commitment, he can let the customer know that he will do all he can to see that the positive characteristics of the borrower’s application are presented fully. Because it may be difficult for a borrower to quickly assemble necessary documentation, a loan originator may occasionally volunteer to perform some of the legwork for a customer, such as picking up needed documents and providing copies. He will track the progress of the application and keep the borrower informed. In addition to the borrower, the real estate agent, seller and lender would all like the loan application to be processed quickly and would like to be kept informed of its progress. Follow-up and communication will keep customers coming back and encourage referrals of business, will generate referrals from other professionals, and will provide the lender with incentive to continue doing business with his mortgage broker.

Duties to the Lender

The mortgage broker must diligently perform the services expected by the lender,
including:

- processing applications based on the lender’s underwriting guidelines.
- following up to ensure conditions contained in commitment letters are satisfied in a timely manner.
- expediting processing so the loan can close within the period of any rate lock.
- carrying out any cancellation procedures competently and professionally.
- guarding against mortgage loan fraud and other practices that may harm the lender or investor purchasing the loan.