SENATE BILL REPORT
SB 6452

As Reported By Senate Committee On:
Consumer Protection & Housing, January 25, 2008

Title: An act relating to requiring certain borrower disclosures of yield spread premiums.

Brief Description: Requiring certain borrower disclosures of yield spread premiums.

Sponsors: Senators Tom, Weinstein, Oemig and Keiser.

Brief History:
Committee Activity: Consumer Protection & Housing: 1/18/08, 1/25/08 [DPS, w/oRec].

SENATE COMMITTEE ON CONSUMER PROTECTION & HOUSING

Majority Report: That Substitute Senate Bill No. 6452 be substituted therefor, and the substitute bill do pass.
Signed by Senators Weinstein, Chair; Kauffman, Vice Chair; Delvin, Haugen, Jacobsen, Kilmer and Tom.

Minority Report: That it be referred without recommendation.
Signed by Senator Honeyford, Ranking Minority Member.

Staff: Vanessa Firnhaber-Baker (786-7471)

Background: A yield spread premium (YSP) is a direct cash payment by a lender to a mortgage broker that is based on the difference between the interest rate at which the broker originates the loan and the market rate at which the lender would otherwise have extended the loan to the borrower.

YSP is permitted under Washington's Mortgage Brokers Practices Act (MBPA) and two federal laws: the Real Estate Settlement Practices Act (RESPA) and the Truth in Lending Act (TILA). These laws also regulate the disclosure of YSP to the borrower. States are permitted to provide additional consumer protections to the borrower as long as they are consistent with RESPA and TILA.

Mortgage brokers are required to provide borrowers with a good faith estimate (GFE) within three days of receiving a loan application. The GFE must include disclosure of all loan terms and fees, including any YSP based on the broker's knowledge of the range of costs. However, the MBPA does not require disclosure of the breakdown of loan fees or points between the mortgage broker and the lender.

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YSP is also disclosed in Section L of the HUD-1 form, which the borrower receives at the closing of the loan as required by federal law. The YSP is listed on the form as a "paid outside of closing" charge.

Mortgage brokers are licensed and regulated by the Department of Financial Institutions (DFI).

Summary of Bill (Recommended Substitute): Mortgage brokers are required to include a breakdown of the loan fees, discount or points between the mortgage broker and the lender in the GFE. The GFE and closing documents must also include the following disclosures: (1) the estimated YSP as an exact dollar amount and not a range; (2) amortization schedules that allow the borrower to compare the total costs and payments of his or her loan when the broker receives a YSP versus when the broker does not receive a YSP; and (3) the transactions' costs that will be incurred by the borrower if the broker receives a YSP, including a higher annual percentage rate or a pre-payment penalty.

DFI must create by rule an amortization schedule to be used in the above disclosure.

A mortgage broker must refund YSP or equivalent compensation directly to the borrower when the estimated YSP in the GFE is lower than what the broker actually receives. The GFE that is used to determine when a refund of YSP must be issued depends on: (1) the length of time between the initial application for a loan and the closing; and (2) whether there has been a reasonable re-disclosure of the GFE. DFI must define "reasonable re-disclosure" by rule. Thus, there are three possible scenarios under which a mortgage broker must refund YSP:

1) A borrower closes on a loan less than thirty days after making an initial loan application and the mortgage broker receives a higher YSP than was disclosed on the GFE.
2) A borrower closes on a loan more than thirty days after making an initial loan application and the mortgage broker receives a higher YSP than was disclosed on a GFE that the borrower received at least 30 days before closing.
3) A borrower closes on a loan in which the broker has made a reasonable re-disclosure of the GFE and the mortgage broker receives a higher YSP than was disclosed on the reasonable re-disclosure.

Loans brokered under the Consumer Loan Act (CLA) are also subject to the disclosures that mortgage brokers must make, including the YSP disclosures.

EFFECT OF CHANGES MADE BY CONSUMER PROTECTION & HOUSING COMMITTEE (Recommended Substitute): Makes technical corrections to align the language with DFI's existing regulations.

Requires mortgage brokers to disclose the borrower's total transaction costs and amortization schedules in addition to YSP.

Alters the GFE that is used depending on the time frame of the loan and whether there has been a reasonable re-disclosure of the GFE to determine when the broker must refund YSP to the borrower.

Amends the CLA to require that loans brokered under the CLA are subject to the disclosures required of mortgage brokers.

Appropriation: None.

Fiscal Note: Requested on January 17, 2008.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony on Original Bill: PRO: Yield spread premium (YSP) is easily disguised; people usually don't even know what YSP is. YSP costs borrowers between 800 dollars and 1,300 dollars on average. More than 75 percent of borrowers could use a less expensive way to pay for closing costs. This bill doesn't prohibit YSP, it just allows consumers to make an informed choice. YSP has its place, but it is rare. Borrowers can't make sound financial decisions unless they know their options and how much their loan actually costs. Brokers know what the YSP will be very early on so it will not be a hardship for them to provide a specific number on the good faith estimate. Disclosure of YSP at closing is too late; it is very hard for a borrower to just walk out of a closing. Some brokers collect both fees and YSP, but borrowers don't even realize it because of inadequate disclosure. YSP is listed as "paid outside closing" on the HUD 1 Form disclosure; this makes borrowers think that YSP does not affect their loan. There are so many closing documents that it is hard for consumers to figure out what is going on.

CON: Disclosures are sufficient currently: a range of YSP is disclosed on an estimate due within three days of the borrower applying for the loan and is disclosed on the HUD form at closing. The credit market is already tight, another disclosure will hurt consumers. Increased disclosure will put brokers at a competitive disadvantage with banks because banks don't have to disclose their profit margin to borrowers. More disclosures will confuse consumers and put doubt in their mind. Requiring a refund of compensation if it is higher than quoted on the original good faith estimate is problematic; brokers should be able to revise the good faith estimate without penalty.

OTHER: There may be some confusion if mortgage bankers are pushed into the mortgage broker category because then mortgage bankers will also have to disclose YSP. This bill could be improved if it also required that brokers disclose to the borrower the relationship between YSP and the interest rate on the loan.

Persons Testifying: PRO: Ari Brown, Brown Sayre Law Group; Kim Justice, Statewide Poverty Action Network; Kim Herman, Washington State Housing Finance Commission.

CON: Jeffrey Lorsch, Washington Association of Mortgage Brokers & Evergreen State Mortgage; Michael Young, Dave Ericksen, Washington Association of Mortgage Brokers.

OTHER: Don Burton, Evergreen Home Loans.