

HOUSE BILL REPORT

SHB 1048

As Passed House:
February 11, 2015

Title: An act relating to updating, clarifying, and strengthening department of financial institutions' enforcement, licensing, and examination statutes relating to residential mortgage lending, and enhancing the crime of mortgage fraud in the residential mortgage lending process.

Brief Description: Updating, clarifying, and strengthening department of financial institutions' enforcement, licensing, and examination statutes relating to residential mortgage lending, and enhancing the crime of mortgage fraud in the residential mortgage lending process.

Sponsors: House Committee on Business & Financial Services (originally sponsored by Representatives Kirby, Stanford, Vick and Ryu; by request of Department of Financial Institutions).

Brief History:

Committee Activity:

Business & Financial Services: 1/13/15, 1/14/15 [DPS].

Floor Activity:

Passed House: 2/11/15, 98-0.

Brief Summary of Substitute Bill

- Authorizes the Director of the Department of Financial Institutions to waive licensing provisions for escrow agents under certain conditions.
- Adds further provisions that constitute the offense of mortgage fraud, specifies venue in mortgage fraud proceedings, and allows civil damages.
- Strengthens enforcement provisions under the Mortgage Broker Practices Act and the Consumer Loan Act, and provides for certain exemptions.
- Makes technical changes to the bill.

HOUSE COMMITTEE ON BUSINESS & FINANCIAL SERVICES

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass.
Signed by 11 members: Representatives Kirby, Chair; Ryu, Vice Chair; Vick, Ranking

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Minority Member; Parker, Assistant Ranking Minority Member; Blake, G. Hunt, Hurst, Kochmar, McCabe, Santos and Stanford.

Staff: Linda Merelle (786-7092).

Background:

Escrow Agent Registration Act.

An escrow agent is a neutral third party that may hold funds or documents or other things of value until the occurrence of a specified event or the performance of a prescribed condition. The escrow agent acts for the purpose of effecting or closing the sale, purchase, exchange, transfer, encumbrance, or lease of real or personal property to another. Escrow agents must be licensed by the Department of Financial Institutions (DFI). The applicant for an escrow agent license must include, among other things, the qualifications and the business history of the applicant and all of its officers, directors, owners, partners, and controlling persons; whether the applicant has been convicted of any crime within the preceding 10 years; and evidence of compliance with the bonding and insurance requirements.

Mortgage Lending and Ownership.

In 2007 the Task Force for Homeowner Security (task force) convened to evaluate instability in the mortgage market and minimize the impact in Washington. The task force made several recommendations, including increasing the penalties for Mortgage Fraud. Many of the task force's recommendations were enacted in 2008.

It is a criminal offense to engage in deceptive practices in connection with making, brokering, obtaining, or modifying a residential mortgage loan. A person commits Mortgage Fraud if he or she materially misleads any borrower or lender during the lending process; knowingly makes any misstatement, misrepresentation, or omission during the mortgage lending process, knowing that it may be relied on by the mortgage lender, borrower, or any other party to the process; or receives proceeds or anything of value in connection with a residential mortgage closing that such person knew resulted from a prohibited misstatement, misrepresentation, or omission. The offense of Mortgage Fraud is a class B felony, which carries a maximum sentence of 10 years and a \$20,000 fine.

Mortgage Broker Practices Act.

The Mortgage Broker Practices Act (MBPA), codified in RCW 19.146, establishes a regulatory and licensing structure for mortgage brokers that is overseen by the DFI. A mortgage broker is any person who assists a person in obtaining or applying to obtain a residential mortgage loan or performs residential mortgage loan modification services or who holds himself or herself out as performing such services and does so for direct or indirect compensation.

Under the MBPA, mortgage brokers must fully disclose the terms of loans, ensure that mortgage broker fees collected for third-party service providers are placed into bank trust accounts, and refrain from engaging in unfair and deceptive acts and practices.

A licensee must provide the Director of the DFI (Director) with an annual report of its mortgage broker activity. The Director may, by rule, create a schedule and format for the annual report. A loan originator may only take an application on behalf of one mortgage broker at a time, and the mortgage broker must be clearly identified on the application.

Consumer Loan Act.

The Consumer Loan Act (CLA) authorizes the DFI to regulate consumer loan companies who conduct business in Washington, and it governs the licensing of mortgage loan originators. Consumer loan companies include mortgage lenders and consumer finance companies. A mortgage loan originator is an individual who takes a residential mortgage loan application or offers or negotiates terms of a residential mortgage loan.

The CLA limits the rates and fees lenders may charge on loans, restricts certain loan provisions such as prepayment penalties, requires lenders to fully disclose the terms of loans, and prohibits lenders from engaging in unfair and deceptive acts and practices.

A violation of either the MBPA or the CLA is a violation of the Washington Consumer Protection Act.

Secure and Fair Enforcement for Mortgage Licensing.

The Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (S.A.F.E. Act) was enacted in 2008 and mandates a nationwide licensing and registration system for residential mortgage loan originators.

Federal National Mortgage Association/Federal Loan Home Mortgage Corporation.

The Federal National Mortgage Association (FNMA, also known as "Fannie Mae") and the Federal Home Loan Mortgage Corporation (FHLMC, also known as "Freddie Mac") are government-sponsored enterprises. They do not lend money directly to home owners, but they buy mortgage loans and mortgage-backed securities for investment.

Summary of Substitute Bill:

Under this bill, the Director is given broader discretion regarding the licensing requirements under the Escrow Agent Registration Act. Also, the licensing, examination, and enforcement provisions of the MBPA and the CLA are amended to be more closely aligned. The bill also incorporates technical changes.

Escrow.

The Escrow Agent Registration Act is amended to authorize the Director to waive the licensing provisions for escrow agents if he or she determines that it is necessary to facilitate commerce or to protect consumers. The Director also has the authority to adopt rules regarding the waiver of licensing provisions.

Mortgage Lending and Fraud.

Definitions.

New definitions are added:

"Mortgage lending process" is the process through which a person seeks or obtains a residential mortgage loan or residential mortgage loan modification. The process may include solicitation, application, negotiation of terms, third-party provider services, underwriting, signing and closing, and funding of the loan.

"Residential mortgage loan modification" is a change in one or more of a residential mortgage loan's terms or conditions. Such change may include forbearances; repayment plans; changes in interest rates, loan terms, or loan types; or reductions of the principal loan amount.

Fraud.

Activity that Constitutes Fraud. The scope of activity encompassed by the fraud statute is widened. It covers any deceptive or misleading acts in connection with the mortgage lending process. Additional activities that will be considered fraud are added:

- filing a document with the county recorder or the official registrar of deeds knowing that the document contains a material misstatement, misrepresentation, or omission;
- actions by third party residential mortgage loan modifiers stated in RCW 31.04.297 (3); or
- knowingly altering, destroying, shredding, mutilating, or concealing a record, document or other object with the intent to impair the investigation and prosecution of Mortgage Fraud.

Venue. The act specifies that the venue for the criminal offense of Mortgage Fraud may be located: in the county in which the residential property for which a residential mortgage loan is being sought; in any county in which any act was performed in furtherance of the violation; or in any county in which a document containing a misstatement, misrepresentation, or omission of a material fact is filed with the county recorder or the official registrar of deeds.

Civil Damages. A person who violates the Mortgage Fraud provisions is liable for civil damages of \$5,000 or actual damages, whichever is greater, including costs to repair the victim's credit record and quiet title on the residential property that is involved in the prosecution, and reasonable attorney's fees, as determined by the court.

Correcting the Public Record. In a criminal case where there has been a conviction for Mortgage Fraud, the sentencing court may issue any orders that are necessary to correct a public record that contains false information resulting from the criminal offense.

Mortgage Broker Practices Act.

Definitions.

Definitions for "license" and "licensee" are added. The definition of a "licensee" includes a person who should have a license. The definition for "independent contractor" is removed, but the term is still used throughout the statute.

Exemptions from Chapter.

Exempt from the provisions of this chapter are nonprofit housing organizations that broker residential mortgage loans under housing programs funded by federal or state programs, in whole or in part, if the primary purpose of the programs is to assist low-income borrowers with purchasing, repairing, or otherwise providing housing for low-income Washington residents.

Mortgage Brokers.

Persons Governed by Chapter.

The scope of persons that may be liable under the provisions of this chapter is expanded to include officers, directors, employees, independent contractors, or any other person subject to the provisions of the chapter. Specific acts may be violations of this chapter whether they are direct or indirect.

Additional Violations.

It is a violation of this chapter to:

- originate loans from any unlicensed location;
- solicit or accept from any borrower any instrument of conveyance of any interest in the borrower's primary dwelling that is subject to one or more mortgage loans at or near the time that the loan interest is taken or in the advance of foreclosure; or
- make a residential mortgage loan unless the loan is table funded; a loan is table-funded when the mortgage broker is named on the mortgage or promissory note as the lender.

Mortgage Broker Licenses.

The Director may waive one or more licensing requirements or permit an applicant to submit other information in place of information required by statute or rule.

Enforcement.

Refunds and Conditions. In addition to imposing fines and restitution, the Director may order refunds against licensees, employees, independent contractors, and agents of licensees. The Director may also condition or decline to reactivate a mortgage broker's or loan originator's license.

Director's Affirmative Actions. In addition to ordering a licensee, its employee, loan originator, independent contractor, agent, or other person to cease and desist from conducting

business, the Director has the discretion to take any other affirmative action as is necessary to comply with this chapter.

Costs and Expenses. Unless, after a hearing, the Director determines that no violation has occurred, he or she may recover the state's costs and expenses for prosecuting violations of this chapter, including staff time spent preparing for and attending administrative hearings and reasonable attorney's fees.

Temporary Cease and Desist Orders.

If the Director determines that there is likely to be substantial delay in issuing a cease and desist order, the Director may issue a temporary order and direct the licensee to discontinue any violation and to take any necessary action to comply with the statutes governing mortgage brokers and loan originators. The order may also include a summary suspension of the licensee's license and may order the licensee to immediately cease the conduct of business.

Licensing.

The Director may require information on an application for a loan originator license to include requirements set by the Nationwide Mortgage Licensing System and Registry, a licensing system developed and maintained by the Conference of State Bank Supervisors.

Consumer Loans.

Definitions.

Some definitions under the CLA are added or modified. A definition is added for an "affiliate" who is any person who directly or indirectly, through one or more intermediaries, controls, or is controlled by, or is under common control with another person.

The definition of "licensee" is modified to include any person, whether located within or outside of Washington, who fails to obtain a required license. The definition of a "loan" is modified to add that it is a transfer of a sum of money "with an expectation of repayment of any amount in excess of the amount transferred."

A "mortgage loan originator" includes persons who, for direct or indirect compensation, hold themselves out to the public as being able to perform the services of a mortgage loan originator and those who perform or hold themselves out to the public as performing residential mortgage loan modification services.

Prerequisites for Licensing.

The Director may deny an application for a mortgage loan originator license if the applicant has been convicted of a gross misdemeanor involving dishonesty or financial misconduct.

The Director may waive one or more application requirements under the CLA or permit the applicant to submit other information in place of the requirements set forth in the statute or in rule.

Exemptions.

Where a person is selling his or her own property and where the property does not contain a dwelling, the owner provides financing for the sale, and the property is the security, the financing is exempt from the CLA. The exemption is available for no more than five transactions in a calendar year, and it does not apply to individuals subject to the S.A.F.E. Act or persons in the construction business or a contractor for the construction of residential dwellings.

Individuals employed by a licensed residential mortgage loan servicing company, where the individual is engaging in activities related to servicing are exempt, unless licensing is required under federal law.

Surety Bond.

Each applicant for a license to be a mortgage loan originator must maintain a surety bond that is continuous. The surety must give notice to the Director upon cancellation of the bond, and the cancellation is effective 45 days after the Director receives notice.

Fees.

A residential mortgage loan servicer may collect fees associated with obtaining a credit report even if the borrower's loan application is not granted.

Enforcement.

Conditions on License. In addition to the power to suspend or revoke a license, the Director may set certain conditions on the license. The Director has this power when a licensee has failed to comply with any directive, order, or subpoena issued by the Director. The Director may exercise this authority with regard to a particular license or all of the licenses issued to the licensee.

Fines. The Director may also impose fines of up to \$100 per day per violation if a licensee, its employee or loan originator, or other person subject to this chapter fails to comply with a directive issued by the Director.

Refunds. In addition to his or her existing powers, the Director may refund all fees received by a licensing through violations under RCW 31.04.

Liquidity, Reserves, and Net Worth. A residential mortgage loan servicer licensee must maintain liquidity, operating reserves, and a tangible net worth in accordance with generally acceptable accounting principles. Residential mortgage loan servicers meet these requirements if they are approved by and meet the standards required by Fannie Mae or Freddie Mac. For loans serviced that would not otherwise be subject to the requirements of

Fannie Mae or Freddie Mac, the servicer must meet the highest standards of the government-sponsored entity or entities for which they are approved.

Receivership. Upon application by the Director and upon a showing that the interest of borrowers or creditors requires such action, the superior court may appoint a receiver to take over, operate, or liquidate any residential mortgage loan servicer.

Investigations. The Director, for the purpose of discovering violations, must have free access to employees, in addition to the physical offices and books, records, and documents. The Director may require by directive, subpoena, or any other lawful means the production of such books, records, documents, and other information to be copied.

Costs and Expenses. The Director may recover the state's costs and expenses for prosecuting violations under the CLA, including staff time spent preparing for and attending administrative hearings and reasonable attorneys' fees unless, after a hearing, the Director determines that no violation has occurred.

Repealed Provisions.

The RCW 19.146.290, regarding the requirement of an annual report of mortgage broker activity, is repealed. The RCW 19.146.330, regarding a limit on applications taken by a loan originator, is also repealed.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony:

(In support) This bill harmonizes the MBPA and the CLA to make the enforcement tools equivalent. The DFI worked closely with prosecutors, and one of the key provisions in the bill relates to the prosecution of Mortgage Fraud offenses. The provisions of this bill clarify who is covered under this bill. Companies that should be licensed but fail to get a license are also subject to the law. Mortgage loan servicers must maintain a consumer loan license under the CLA. The number of loans serviced has increased dramatically through the years. There are provisions to assure that the licensees remain solvent and to better protect Washington consumers. The receivership provisions will allow the DFI to go to court and get a receiver appointed. This bill will strengthen the ability to prosecute Mortgage Fraud and improve the enforcement of protections for victims. Some of the new provisions will save the courts time and money in addressing matters during the criminal proceeding rather than requiring additional civil proceedings. There is a convergence of interests. The bill will help consumers stay in their homes and to repair their credit, and this would help the industry as well. The court-ordered provisions contained in the bill would also allow consumers to clear up chain-of-title issues that arise.

(Opposed) None.

Persons Testifying: Representative Kirby, prime sponsor; Charlie Clark, Department of Financial Institutions; Jennifer Atchison and Hugo Torres, King County Prosecutor's Office.

Persons Signed In To Testify But Not Testifying: None.