 By Edgar Bright, CMB

Is the Medicine Hurting the Patient?

About a year ago, I suggested in this magazine that there were valuable lessons about recovery from Hurricane Katrina to be learned by our government in the face of a growing national recession and an unprecedented mortgage crisis. As an owner and president of an independent mortgage banking company affected by both events, I am disappointed that what I feared most from the "rulemakers" is actually happening.

Although reform was definitely in order, overreaction has dominated, and the result is a measurable increase in the costs of obtaining a mortgage and a decrease in single-family housing transactions. We are now dealing with an overdose of new and sometimes biased legislation and regulation. Much like a natural disaster, those most affected are borrowers, housing itself and companies like mine that bring the two together.

My company is the largest independent mortgage banker domiciled and servicing loans in the Gulf Coast region during two of the worst disasters in U.S. history. Following Hurricane Katrina, we were faced with the mixed challenge of managing a recovery plan that would restore value to our asset and save our company, but not at the expense of borrowers suffering from the same disaster. It is too early to assess the effects of the other disaster—the BP oil spill.

Let me say very early in this column that this is not a discussion of the effects of Hurricane Katrina; we are moving on as a company and a city. A high-ranking executive with a governmental lending agency told us very bluntly that "everyone has a story," so my references to Hurricane Katrina are not for pity but rather for comparison.

It is true that, though far from perfect, the Katrina recovery plan was considerate of all of the participants affected by the disaster, while knowing that revival of the borrower needed to be kept at the forefront. By the way, the participants included government, investors, insurers, lenders and borrowers. Sound familiar? I fear that this time around as regulators attempt to medicate and revive the borrower in today's ailing housing market by overregulating the lender, they are in fact "hurting the patient."

The overdose

Although many of the new Real Estate Settlement Procedures Act (RESPA), disclosure and compliance requirements are complex, time-consuming and costly for lenders, they are at least consistent across all mortgage channels. Regulations created by Congress, the Department of Housing and Urban Development (HUD) and the government-sponsored enterprises (GSEs)—such as The Home Valuation Code of Conduct (HVCC), the Mortgage Disclosure Improvement Act (MDIA) and the 2008 RESPA rule, and this years' Loan Quality Initiative (LQI)—have put the mortgage industry on its heels.

Adherence to and management of the onslaught of new regulation will create monetary and non-monetary negatives for quite some time. While designed to be protective of the borrower and punitive for the lender, the complexity and increased transaction costs may actually end up hurting the borrower.

Has the SAFE Act created an unsafe harbor?

As a company, we are accepting of and adhering to the barrage of new regulations and the increased resources and costs associated with them. We are not so calm in accepting the ramifications of the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act) passed by Congress and HUD's expansion of this biased legislation.

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In general, we agree with the SAFE Act's core platform of "uniform certification." It is a validation that supports origination as a career rather than a job. We also agree that the direct costs (an average of nearly $500 per originator) and the management of the licensing function, although very costly, is the responsibility of the company employing these specialists.

Yet, I strongly disagree with the loophole created for depository institutions under the SAFE Act. By allowing the exemption for bank loan officers to become registrants in lieu of licensure, the underlying goal of consumer protection by certification is compromised in an arena where bank lenders hold a dominant market share. Additionally, a competitive hiring advantage for depository institutions has ironically provided safe harbor for originators that fail or escape the licensing requirement, and an "unsafe harbor" for borrowers.

If the SAFE Act and licensure of originators was one remedy to cure the ills of unsafe lending, its exemption for the largest segment of the mortgage market (depository lenders) is a roadblock to success and a catalyst for a more costly transaction.

The anecdote

As independent mortgage bankers, we strongly agree that universal reform was in order for the real estate market and mortgage transaction. We also agree that purging the industry of participants that make bad decisions and do harmful things was appropriate. On the other hand, we disagree with regulation that is incomplete and inconsistent, ignores the poor decisions by nonlender participants and fails to address the shortcomings of the process with equality. This, in essence, becomes just another bad decision.

Instead, we would advocate that the rulemakers administer the remedy with balance across all participation lines and with no preconception that the symptoms reside in only one channel.

There is no doubt that on the street, the best medicine recently for the housing market has been government's strategy of buying bonds to affect long-term interest rates, as well as the homebuyer tax-credit legislation to reduce housing inventory. The next best move would be to consider a mild softening of underwriting standards for loans guaranteed by Fannie Mae and Freddie Mac and insured by the private mortgage insurance companies.

As in the recovery following Katrina, the greatest emphasis was put on those most severely affected, and that was certainly appropriate. However, we were also very diligent not to ignore the moderate casualties as they attempted to return to their homes. In some ways, we are witnessing a borrower population that is being penalized today as a result of regulatory and risk overreaction.

As we see it, the combination of low rates, broad-based tax incentives and realignment of risk assessment is the best medicine for a balanced recovery. We also suggest that broader solicitation of research and ideas from the front lines can result in a safe and compliant mortgage transaction with a clean (and less costly) bill of health.

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