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BILL ANALYSIS



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Senate Bill 871 (Substitute S-1 as reported)
 Sponsor: Senator Michael J. Bouchard
 Committee: Financial Services

Date Completed: 3-5-96

RATIONALE

The Mortgage Brokers, Lenders, and Servicers Licensing Act was enacted in 1987 in response to serious abuses of mortgage borrowers and investors in the early and mid-1980s. According to the Financial Institutions Bureau (FIB), one firm alone cost Michigan investors, many of whom were retired and living on fixed incomes, a total of about \$44 million. The Act's regulatory program was designed to be self-funded by license fees and examination and investigation fees. Since the Act sets equal annual fees for licensees, regardless of the size of their operations, and allows hourly fees for staff time involved in the examination of a licensee or investigation of a registrant or licensee, the FIB, in effect, must examine every licensee yearly, whether an examination is warranted or not, in order for the regulatory program to remain financially self-reliant. Some people believe that the State should implement a new regulatory fee structure that would assess varying annual fees on licensees and registrants, depending on their volume of business, to allow the program to continue to be self-sufficient, but enable the FIB to concentrate examinations and investigations where they are most needed.

In addition, the Act has not been revised substantially since its enactment. In that time, the mortgage market has continued to evolve and some feel that some aspects of the Act's regulatory program impede lenders' ability to participate in certain business practices related to secondary mortgage markets and limit their ability to collect some costs associated with making or servicing a loan.

CONTENT

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

- **Revise certain licensure and registration requirements.**
- **Revise the Act's financial responsibility and net worth requirements.**
- **Restructure the Act's fee requirements, including creating a volume-based annual operating fee.**
- **Revise the Act's examination and investigation provisions.**
- **Revise the Act's violation provisions, including prohibiting exclusive business requirements, security interests taken before closing, and misleading advertising practices.**
- **Require that the terms and conditions of a guaranteed rate of interest be specified in writing.**
- **Revise the Act's list of entities exempted from its regulation.**
- **Permit the transfer or assignment of certain loans before the disbursement of 75% of the loan's proceeds to, or for the benefit of, the borrower.**
- **Allow the Commissioner of the Financial Institutions Bureau to require a licensee or registrant to make restitution for violations of the Act.**
- **Make other provisions pertaining to use of the word "bank", delivery to the FIB Commissioner of an annual financial statement, and the payment by a borrower of reasonable and necessary charges.**

Licensure and Registration

Within 90 days after the bill's effective date, a person that was licensed to make regulatory loans under the Regulatory Loan Act or was licensed to make secondary mortgage loans under the secondary mortgage loan Act, and who was registered with the FIB Commissioner under the Mortgage Brokers, Lenders, and Servicers Licensing Act, would have to file with the Commissioner an application for licensure or discontinue all activities subject to that Act's regulation.

Similarly, within 90 days after the bill's effective date, a mortgage broker, lender, or servicer who was exempt from regulation under the Act, and who was a subsidiary or affiliate of a depository financial institution or of a depository financial institution holding company, would have to register under the Act or discontinue all activities subject to the Act's regulation if the depository financial institution or holding company did not maintain a main office or branch office in Michigan.

Under the Act, a real estate broker or real estate salesperson 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 those services additional compensation beyond the customary commission on real estate sales is exempt from licensing and registration requirements for that 12-month period. The bill provides that, if the broker and all real estate salespersons affiliated with the broker, in aggregate, brokered more than 30 mortgage loans in the same 12-month period, the broker would have to obtain a license or would have to register as otherwise required by the Act.

The bill specifies that a license issued or registration accepted by the FIB Commissioner would not approve the use of or indemnify the licensee or registrant against claims for the improper use of the business name stated in the license or registration.

The Act allows a licensee or registrant to surrender a license or registration by delivering it to the FIB Commissioner with a written notice of surrender. The bill specifies that a licensee or registrant whose license or registration had been destroyed or lost could comply with the surrender requirement by submitting to the Commissioner a notarized affidavit of the loss accompanied by written notice of surrender.

Financial Responsibility and Net Worth

Financial Responsibility. The Act requires that an applicant for licensure or renewal of a license "deposit" certain amounts with the FIB Commissioner as proof of financial responsibility. An applicant who acts as a mortgage broker and who receives funds from a prospective borrower before the closing of the mortgage loan or who acts as a mortgage lender must deposit \$15,000; an applicant who acts as a mortgage servicer must deposit \$100,000. The deposit may take the form of a corporate surety bond or a letter of credit. The bill would require that an applicant "provide" proof of financial responsibility, in the form of a surety bond or letter of credit, and would increase the amounts to \$25,000 and \$125,000, respectively.

In place of depositing a surety bond or letter of credit, the Act allows an applicant to deposit with the State Treasurer either certain U.S. or state obligations, guaranteed fully as to principal and interest, or a certificate of deposit of a Federally insured financial institution. The bill, in addition, would require a nonrefundable administrative fee established by the FIB Commissioner, not to exceed \$100.

The bill would delete a provision that exempts from the financial responsibility requirements a mortgage broker who deposits all funds received from a prospective borrower into an escrow account and does not possess or control the funds associated with the loan application before the closing or denial of the loan, or who submits to the Commissioner an opinion by a certified public accountant verifying a net worth required under the Act.

The bill would require the FIB Commissioner to prioritize and pay claims against a proof of financial responsibility, filed under the Act, in a manner that, in the Commissioner's discretion, best protected the public interest. Claims could be filed against a licensee's proof of financial responsibility only by the licensee's borrowers, mortgage loan applicants, loan servicing customers, and the Commissioner. If valid claims exceeded the amount of the proof of financial responsibility, each claimant would be entitled only to a pro rata amount of his or her valid claim.

Claims filed by a borrower or loan applicant could involve only mortgage loans or mortgage applications secured or to be secured by residential real property located in Michigan. The

amount of the claim could not exceed actual fees in connection with a loan application, overcharges of principal and interest, and excess escrow collections charged by the licensee and paid by the claimant to the licensee.

The FIB Commissioner could file a claim for payment of fines or fees due and payable to the Commissioner or the FIB and reimbursement of expenses incurred in investigating the licensee and expenses incurred in distributing proceeds of the proof of financial responsibility. A claim filed by the Commissioner would have to be paid in full before payment of other claims against a proof of financial responsibility, unless the Commissioner, in his or her discretion, waived in whole or in part the right to priority of payment.

Net Worth. The Act requires that a licensee who acts as a mortgage broker and receives funds from a prospective borrower before the closing of the mortgage loan, or a licensee who acts as a mortgage lender, have a minimum net worth in an amount determined by the FIB Commissioner not exceeding \$25,000. The bill, instead, would require those mortgage brokers and mortgage lenders to maintain a net worth of not less than \$25,000. (The bill would retain a requirement that a mortgage servicer have a net worth in an amount determined by the Commissioner not exceeding \$100,000.) The Act requires that net worth be computed in accordance with generally accepted accounting principles. The bill would add a requirement that net worth be disclosed on a form prescribed by the Commissioner or on a form prepared or reviewed by a certified public accountant.

Fee Requirements

“Operating” Fee. The Act requires that, at the time of making an initial application for a license, and at the time of making the first application for a license after the suspension or revocation of a license, the applicant pay to the FIB Commissioner a fee for investigating the applicant and an annual license fee. The bill, instead of an annual “license” fee, would require the payment of the minimum annual “operating” fee. Similarly, a registrant must pay an annual “registration” fee, but the bill would require an annual “operating” fee, instead.

The Act requires the FIB Commissioner annually to establish a schedule of fees sufficient to pay the FIB’s costs of administering the Act. The bill provides that the fee schedule would have to be sufficient to pay, “but not to exceed”, the FIB’s “reasonably anticipated” costs of administering the Act.

Investigation and Examination Fees. Under the Act, the fee for investigation of an applicant for a license must be not less than \$200 or more than \$600, except for mortgage servicers who service between 75 and 200 land contracts, whose investigation fee must not be less than \$200 or more than \$400 after a four-year freeze. All subsequent increases are limited to \$50 per year until the maximum allowable level is reached. Under the bill, instead, the fee for investigation of an applicant could be not less than \$400 or more than \$1,000.

The bill would delete a provision allowing a fee of not less than \$40 or more than \$70 per hour for each examiner involved in the examination of a licensee or investigation of a registrant or licensee. The bill would retain a requirement that a licensee pay the actual travel, lodging, and meal expenses incurred by FIB employees who travel out of State to examine records of a licensee, however, and would extend that requirement to registrants.

Annual Operating Fees. The bill would delete a requirement that, for the issuance or annual renewal of a license or registration, there be a fee of not less than \$300 or more than \$800, except for those mortgage servicers who service between 75 and 200 land contracts, whose annual renewal fee must be not less than \$300 or more than \$500 after a four-year freeze. The deleted provision specifies that all subsequent increases are limited to \$50 per year until the maximum allowable level is reached.

The bill provides, instead, that a licensee or registrant annually would have to pay an operating fee based on the number of closed mortgage loans the licensee or registrant brokered to other parties, the number of mortgage loans closed by the licensee or registrant during the previous calendar year, and the dollar volume of loans serviced by the licensee or registrant as of December 31 of the previous calendar year. The operating fee during the first year after the bill’s enactment could not be less than \$500 or more than \$2,500. Subsequently, in the Commissioner’s discretion, the maximum operating fee could be increased at an annual rate of not more than 10% in the second, third, and fourth years following the bill’s enactment, and in the fifth and subsequent years, at an annual rate of not more than 5%.

Amending Fees. The Act requires that, for amending a license or registration, there be a fee of not less than \$20 or more than \$75. The bill would increase that fee to not less than \$50 or more than \$200, and would apply it to amending or reissuing a license or registration.

Examinations and Investigations

The Act provides that information obtained during an examination or investigation is confidential and cannot be available for public inspection or copying, or divulged to any person, except as specifically allowed in the Act. The bill would delete from the list of exceptions information disclosed under subpoena, to any party in a private action.

The bill would delete a provision that, except as otherwise provided by the Act, the FIB Commissioner may only conduct one examination of a licensee in any 12-month period from July 1 to June 30 and that the cost of one examination must be assessed to the licensee. Instead, the bill provides that, unless circumstances warranted additional examination, the Commissioner would be entitled to conduct one examination of each licensee during the calendar year.

The bill would delete a provision that a licensee or registrant who is investigated after a complaint has been filed must only pay the cost of the investigation if the licensee or registrant repeatedly violates a material provision of the Act. The deleted provision also requires that, to avoid unnecessary duplication, the Commissioner cooperate with any agency of the State or Federal government, other states, the Federal National Mortgage Association, or the Federal Home Loan Mortgage Corporation and accept examination of those entities in connection with, or in place of, an examination by the Commissioner.

Violations

It is a violation of the Act for a licensee or registrant to suppress or withhold from the FIB Commissioner any information that the licensee or registrant possesses and that, if submitted, would have made the licensee or registrant ineligible for licensing or registration. The bill would add to that violation the suppression or withholding of information that would have warranted the Commissioner's denial of a license application or refusal to accept a registration.

Under the Act, it is a violation for a licensee or registrant to fail to place in escrow any money, funds, deposits, checks, drafts, or other negotiable instruments entrusted to the person as a mortgage broker, lender, or servicer, or to fail to deposit and retain the funds in a trust or escrow account maintained with a financial institution whose deposits are insured by the Federal Deposit Insurance Corporation, the Federal Savings and Loan Insurance Corporation, or the National Credit

Union Share Insurance Fund, until the proper disbursement. The bill would delete that language and provides, instead, that, until proper disbursement was made, it would be a violation for a licensee or registrant to fail to place in a trust or escrow account held by a Federally insured depository financial institution, in a manner approved by the FIB Commissioner, any money, funds, deposits, checks, drafts, or other negotiable instruments received that were the portion of a payment on a mortgage loan that the person was obligated to pay to a third party. This would include amounts paid to the holder of the mortgage loan, amounts for property taxes and insurance premiums, or amounts paid under an agreement requiring that, if the mortgage loan were not closed, the amounts paid be refunded to the prospective borrower or, if the mortgage loan were closed, the amounts paid be applied to closing fees and costs. Fees and costs would not include amounts paid to cover costs incurred to process a mortgage loan application, to obtain an appraisal, or to receive a credit report.

Under the bill, it would be a violation of the Act for a licensee or registrant to do either of the following:

- Require a prospective borrower to deal exclusively with the licensee or registrant in regard to a mortgage loan application.
- Take a security interest in real property before closing a mortgage loan to secure payment of fees assessed in connection with a mortgage loan application.

In addition, the bill would prohibit a licensee or registrant from, directly or indirectly, making a false, misleading, or deceptive advertisement regarding mortgage loans or the availability of mortgage loans. A licensee also could not advertise any size of loan, security required for a loan, rate of charge, or other condition of lending, except with the full intent of making loans at those rates, or lower rates, and under those conditions, to mortgage loan applicants who met the standards or qualifications prescribed by the licensee.

Guaranteed Rates

If a licensee or registrant assessed or accepted a fee to guarantee a specified rate of interest on a mortgage loan, the licensee or registrant would have to specify the terms and conditions of the guarantee in writing. The terms and conditions of the guarantee could not extend beyond the guarantee's expiration, unless it were extended in writing by all the parties.

Exemptions

The bill would delete from the Act's list of entities exempted from its regulation a home improvement installment contract entered into pursuant to the Home Improvement Finance Act.

In addition, the Act exempts a mortgage lender that makes 10 or fewer mortgage loans and a mortgage servicer that services 10 or fewer mortgage loans, in a 12-month period from July 1 to June 30. The bill specifies that those exemptions would apply if the lender or servicer, in the aggregate with any affiliates, made or serviced 10 or fewer mortgage loans. The Act also exempts a mortgage servicer that services 75 or fewer land contracts, of which 10 or fewer require the collection of money for the payment of taxes or insurance. The bill specifies that that exemption would apply if the servicer, in the aggregate with any affiliates, serviced 75 or fewer land contracts, of which 10 or fewer required the collection of money for the payment of taxes or insurance.

The Act also exempts a mortgage broker, lender, or servicer that is a subsidiary or affiliate of a depository financial institution or a subsidiary or affiliate of a holding company of a depository financial institution. The bill would limit that exemption to a broker, lender, or servicer that was a subsidiary or affiliate of a depository financial institution that maintained its main office or a branch office within Michigan.

Transfer or Assignment

It is a criminal violation of the Act for a person willfully or intentionally to transfer or assign a mortgage loan or a security directly representing an interest in one or more mortgage loans, other than a land contract not considered to be an equitable mortgage, before the disbursement of 75% or more of the proceeds of the mortgage loan to, or for the benefit of, the borrower. The bill would exclude from that violation a loan made under a State or Federal government program that allowed the lender to escrow more than 25% of the loan proceeds for a limited period of time, and a construction loan.

Restitution

If the FIB Commissioner finds that a licensee or registrant has violated the Act or rules promulgated under it, he or she may assess a civil fine of up to \$1,000 for each violation, up to \$10,000 per person, and/or suspend or revoke the license or registration or refuse to issue or renew

a license. The bill would add the third option of requiring the licensee or registrant, or a person who controlled the licensee or registrant, to make restitution to each injured individual, if the Commissioner found that the violation resulted in an injury to one or more individuals.

Other Provisions

"Bank". Under the bill, except for a State- or nationally chartered bank, savings bank, or an affiliate of a bank or savings bank, a person subject to the Act could not include in its name or assumed name, the words "bank", "banker", "banking", "banc", "bankcorp", "bancorp", or any other words or phrases that would imply that the person was a bank, was engaged in the business of banking, or was affiliated with a bank or savings bank. It would not be a violation for a licensee or registrant to use the term "mortgage banker" or "mortgage banking" in its name or assumed name. A person subject to the Act whose name or assumed name contained a prohibited word on January 1, 1995, could continue to use the name or assumed name.

Financial Statement. Within 75 days after the close of a licensee's fiscal year, the licensee must deliver to the FIB Commissioner a financial statement prepared from the licensee's books and records. The bill would extend the deadline for delivery of a financial statement to 90 days after the close of the fiscal year and apply the requirement to registrants as well as licensees.

Reasonable and Necessary Charges. The Act allows a licensee or registrant to require a borrower to pay "reasonable and necessary charges" that are the actual expenses incurred by the licensee or registrant in connection with the making, closing, disbursing, extending, readjusting, or renewing of a mortgage loan. The bill would add "and a loan processing fee".

The bill would delete a provision that reasonable and necessary charges consist of "recording fees, title examination, or title insurance, the preparation of a deed, appraisal, or credit report, and a loan processing fee".

MCL 445.1651a et al.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The bill's proposed fee structure would eliminate the FIB's reliance on examination revenue to fund the Act's regulatory program. The volume-based annual operating fee would apportion the cost of enforcement more equitably among licensees and registrants and give the FIB greater flexibility in targeting investigations and examinations to deal more effectively with regulatory problems as they arise.

Supporting Argument

Certain aspects of the Act's regulatory structure have impeded licensees' and registrants' ability to operate in the growing secondary mortgage market. For instance, the Act's prohibition against transferring or assigning a mortgage loan to a third party before disbursement of 75% of the loan's proceeds to the borrower has limited lenders' ability to participate in some government loan programs that allow the lender to escrow more than 25% of the loan proceeds for a limited period of time. The same prohibition also can hinder licensees' and registrants' participation in the secondary mortgage market for construction loans, which typically are approved and closed before completion of the construction, but might not be quickly disbursed.

In addition, the Act allows a licensee or registrant to require that a borrower 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 Act's list of what constitutes "reasonable and necessary charges" is limiting, however, and may actually exclude some legitimate costs. The bill would address this problem by retaining the authorization to assess reasonable and necessary charges, but deleting the laundry list of types of charges.

Supporting Argument

The bill would increase the required bond amounts to demonstrate financial responsibility. According to testimony before the Senate Financial Services Committee, the bill's proposed bond requirements reflect the amounts originally required when the Act became law in 1987. At that time, however, surety companies apparently were reluctant to write bonds for licensees because of previous abuses in the mortgage industry. Consequently, the bonding requirements were soon reduced. The bill would increase those amounts back to their original levels.

Legislative Analyst: P. Affholter

FISCAL IMPACT

This bill would continue the trend of making mortgage regulation a self-funded program. Under the current system, both license fees and examination fees fund the enforcement activities necessary to regulate this industry. All licensed or registered companies pay the same fee regardless of size or revenue. Under the proposed system the above fees would be eliminated and an operating fee would be introduced to replace them. The operating fee would be set for each company based on the number of mortgages closed and the dollar value of the loans serviced. This new fee would have to be not less than \$500 and not more than \$2,500, which would increase the current revenue for this program by an estimated \$150,000 to \$200,000.

Fiscal Analyst: M. Barsch

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.