

January 2017

# State of the Industry



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# LETTER FROM THE SPONSOR



Good, bad or indifferent, 2017 promises to be a very interesting year. With rising rates, political uncertainty, and the future impact of the CFPB along with the Dodd-Frank legislation, our industry has many open-ended questions.

However, 2017 for our industry appears to be on pace to maintain its upward trajectory. What we can count on is that purchase business will thrive as demand continues to increase. Due to the implementation of Best Practices, we are now more financially transparent and secure than at any other time in our industry's history.

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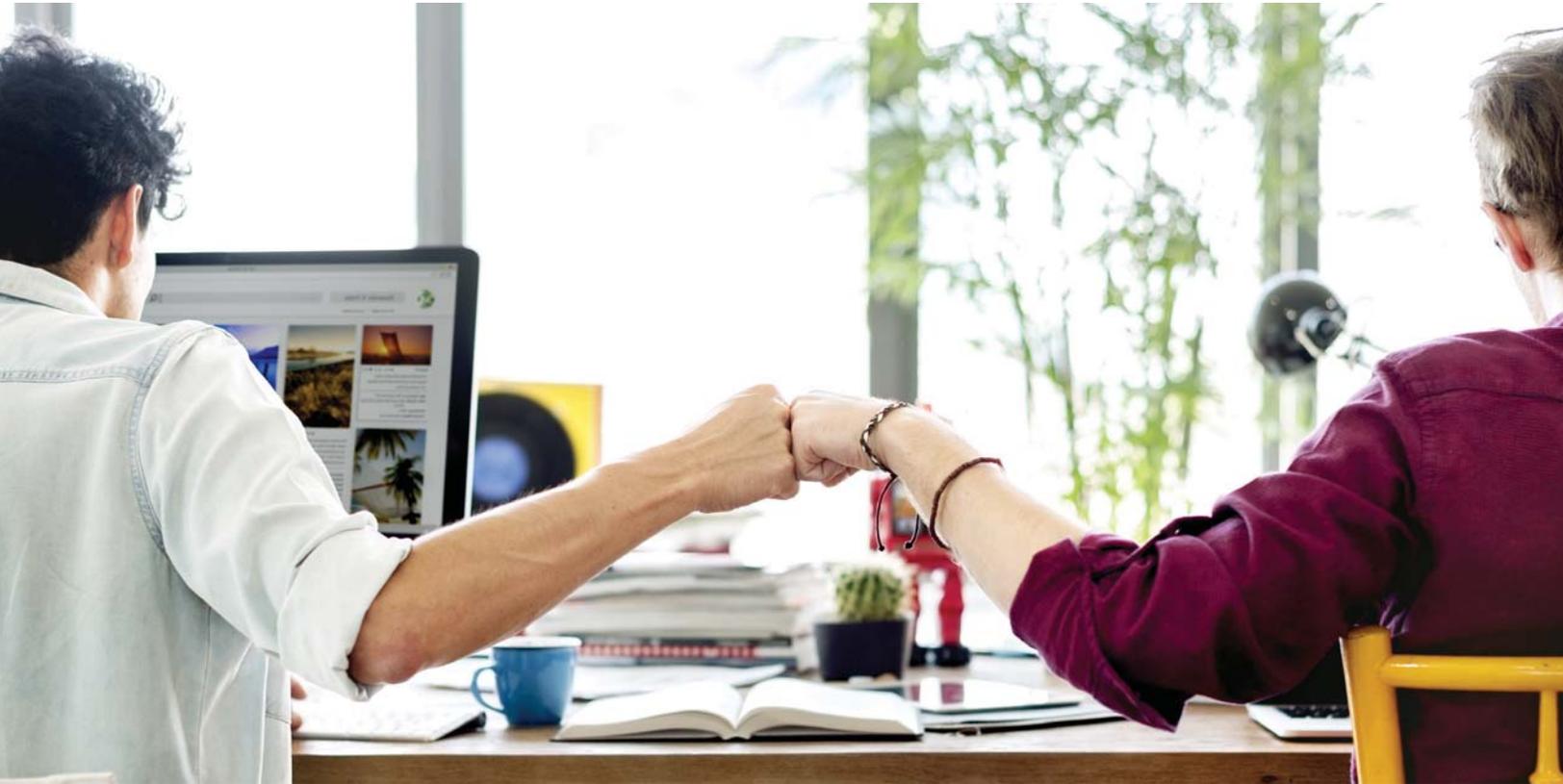
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# Despite uncertainty, economists expect industry to build on 2016 growth

By Chris Freeman — *Editorial Director*

Economic experts are forecasting a future so bright that housing industry participants might need to wear shades.

Economists from the Mortgage Bankers Association (MBA) and Fannie Mae said they expect to see continued growth in the economy in 2017, leading to growth in the mortgage and housing markets as well.

Fannie Mae forecasts a 3 percent rise in home sales in 2017 from a year earlier, including a 15 percent increase in single-family housing starts and nearly 13 percent growth in new single-family home sales.

MBA forecasts purchase originations to total \$1.1 trillion in 2017, the first time it will have passed the \$1 trillion mark since 2007.

“We are projecting a very strong purchase market next year, the highest purchase volume since 2007,” MBA Chief Economist **Michael Fratantoni** told October Research, LLC. “That’s good news for the industry. That’s going to come in the context of a still-improving job market. Economic backdrop ... really quite positive.”

Economic fundamentals point to modest growth in 2017, both groups said. Fannie Mae forecasts GDP growth of 2.2 percent in 2017, up from a 1.5 percent forecast for 2016. Both organizations expect the unemployment rate to be 4.6 percent.

The National Association of Realtors (NAR), meanwhile, forecasts existing-home sales to finish

at 5.36 million units in 2016, which would be the industry’s best year since 2006. NAR’s forecast calls for 2 percent growth in home sales next year, on top of what has been the industry’s best performance in a decade.

“The gradually expanding economy, multiple years of steady job creation and mortgage rates under 4 percent all contributed to sizeable interest in buying a home this year,” NAR Chief Economist **Lawrence Yun** said.

Home prices, which have risen nationwide to levels last seen before the Great Recession, are expected to increase again in 2017. NAR forecasts a 4.2 percent increase, MBA sees it at 4.9 percent and Fannie Mae has it up 4.7 percent.

Still, MBA Vice President of Research and Economics **Lynn Fisher** told October Research that the housing market does not show signs of reaching 2005-2006 bubble levels.

“My idea of a bubble is that housing prices are rising for reasons that are outside of the economic fundamentals. And what we’re talking about here is that that isn’t happening,” she said. “On the single-family side it’s hard for me to talk about the bubble when in fact it’s being driven by true demand. A bubble is when it’s not substantiated by demand. From my point of view you need house prices to go up because you need that to trigger redevelopment.”

## Making money

Strong sales in 2016 have led to profitable results for the mortgage industry. MBA Vice President of Industry Analysis Research and Economics **Marina Walsh** told October Research that mortgage profits were on the rise.

“This has been a pretty good year for the mortgage lenders on the production side at least,” she said. “In the second quarter of 2016, based on our most recent quarterly performance report, we were at 73 basis points (pre-tax profit), which is really strong. That translates into about \$1,700 per loan in net profit overall.”

That growth continued into the third quarter report, which showed a pre-tax profit of 74 basis points, translating to \$1,773 per loan, up nearly \$100 a loan from the \$1,686 registered in the second quarter.

That has come despite the fact that the industry is near all-time highs in average expenses for producing a loan, dating back to the start of MBA’s reporting on the issue in 2008.

“If you look over that time, average expenses were about \$5,800 per loan. For the past 12 quarters we’ve been above that, so in essence we’ve had revenues that have been able to withstand the increase in production expenses,” Walsh said. “And that has been an important part of the profitability of mortgage lenders is to have that revenue, largely on a per-loan basis, helped by rising loan counts overall. So rising loan counts [are] bringing up the revenue. We’re almost at an all-time high ... we’re in a pretty high expense environment at about \$7,200 per loan in production expenses.”

As expenses for producing mortgage loans have risen over the years, though, compliance costs have been at the forefront of the industry, Walsh said.

“The cost of compliance is the No. 1 question we seem to be getting over the last two or three years. What is the variance, what is the change in cost to comply,” she said. “In terms of overall fulfillment cost, it ranges from about \$900-\$1,200 of the additional cost added, but it’s really tough to isolate cost of compliance.”

Mortgage lenders also are making profits on the

# A Look Ahead

Here’s a look at some of the 2017 forecasts by the top economic groups in the industry.

## HOME SALES

Up 3.0% to 6.133 million units

(Source: Fannie Mae)

## GDP

Up 2.2%

(Source: Fannie Mae)

## HOME PRICES

Up 4.9%

(Source: Mortgage Bankers Assoc.)

## UNEMPLOYMENT RATE

4.6%

(Source: Fannie Mae)

## HOUSING STARTS

Up 5.3% to 1.22 million units

(Source: National Assoc. of Realtors)

## MORTGAGE RATE

4.2% for 30-year fixed rate

(Source: Mortgage Bankers Assoc.)

servicing side of the industry, Walsh said.

“On the servicing side, the numbers are looking great. We’re at a 10-year low for the overall delinquency rate, the loans in foreclosures are at the lowest rate since 2000, so a lot of positive news in terms of the overall performance,” she said.

There are a host of reasons for growth, MBA economic officials said. The growth of household formation and a diversifying demographic is among the top reasons.

“The demographics are quite positive. We think there could be as many as 1.6 million households a year over the next decade going forward,” Fisher said. “The growth is coming among young people and those over 60.”

“The pace of household formation has picked up and we expect it to continue for the next decade,” Fratantoni added.

## Unclear path ahead

Deciding just how growth will look in 2017 has been tricky, Fratantoni said, particularly as the election season wound down to November.

“It’s definitely one of the bigger sources of uncertainty this year. In many ways (CEOs) are sitting on their hands right now in terms of do you make that investment in your plant, and I think a lot of them were waiting to see the outcome of the election. And you see it in the macroeconomic numbers that business investment is down,” he said. “What’s baked into our forecast is something similar (to now), and that means higher costs on the origination and servicing side, along with the regulatory framework we have in place now.”

Fannie Mae Chief Economist **Doug Duncan** said one of the difficulties in gauging the forecast is weighing the unknowns. He said his staff at the Economic and Strategic Research Group looked to the last election cycle to help gauge the future.

“You have to attend to things which are known. We know a budget agreement has to be reached. The last time we were here was 2012 and the theme of 2012 was that it was the year of the political economy,” Duncan told October Research. “We had the fiscal cliff debate first. The second thing was it was a presidential/congressional year and that affected the environment of policy development. The third thing was the economic profession did a disservice by suggesting that the political environment shouldn’t

affect economic analysis. We don’t view that as being impure; everything they do in the political realm has an effect on the economic.

“I have no idea what to conclude,” Duncan added. “Macroeconomics is as much art as science. They’re trying to make an educated guess. It gives you a framework for things of things, but then you apply judgment to that.”

Fisher said one of the potential drivers in an increasing purchase origination market will be work by Fannie Mae and Freddie Mac on affordable loans. The government-sponsored entities (GSEs) launched programs in the past two years to open the credit box, but Fisher said the fruits of that labor might just be starting to show. She referenced MBA research to see what aggregators and investors are doing in the market.

“Nearly 60 percent of them are offering some program around GSE’s affordable 97 percent loan-to-value ratio programs. To the extent that the GSEs have opened the doors to those things, investors and aggregators have (responded),” Fisher said.

Yet originators have not taken advantage of many of those opportunities.

“There’s been a slower uptake at the actual point of origination. So there’s some uncertainty about why exactly that is,” she said. “Certain people in the market are so used to going to an FHA product that we saw a big marketing push by the GSEs, so it’s a little bit about getting the message out there. The loan originators are just starting to take a look at it, so we think there’s actually some potential there.”

Finally, mortgage rates are expected to rise, albeit moderately, in 2017. Fratantoni said MBA has predicted such for years now, but global events have kept rates unexpectedly low. In 2017, he said that is expected to change.

“The Fed is likely to raise rates. We have in our forecast the Fed is likely to raise rates three times next year. We see them continuing to raise their short-term rates over the next couple of years,” he said. “Probably the more important rate for us is the mortgage rate, and that’s going to go up but much more slowly.

“We have been forecasting rising mortgage rates for years now, we’ll freely admit that. What’s caught us by surprise each time has been one global event or another. There certainly are events out there that could cause rates to drop ... but it’s difficult to predict what they might be. But what we think is the most likely outcome is for long-term rates to rise moderately.”

# Title experts bullish after strong 2016

By Tara Quinn — Editor, *The Title Report*

According to industry insiders, 2016 was an incredible year for the industry. Westcor CEO **Mary O'Donnell** said it is going in the history books as the underwriter's biggest year ever.

"From a gross revenue perspective we're up 38 percent over last year, which is a huge increase for us," she said. "We've seen a shift to a purchase-driven market. That has really played to our strengths and to the benefit of our agents."

In 2016, Westcor completed many initiatives. It added an investor services group. Its focus is on title and curative work for portfolio buyers of non-performing loans and single family rental properties. It also expanded the use of its formerly acquired data analytics company as well as Realty Data Company, a traditional search company it acquired in 2015. To support the growth Westcor doubled the size of its IT department in 2016 and added approximately 100 staff members.

Fortune Title CEO **Nicole Plath** also reported a strong 2016. She said the amount of settlements has gone "through the roof."

"Our biggest uptick has been in REO properties," she said. "New Jersey has the highest rate of foreclosures in the country. This is because we're a judicial state and during the housing crash we had cases surrounding the information on the Notice of Intent that went up to the Supreme Court, causing a hold on the majority of foreclosures in the state for over 2 years. We're continuing to feel the effects of that now. Properties that were in default as early as 2009 are being foreclosed today. Once the foreclosure is complete and the bank owns the property, they order a Preliminary Title Report to ascertain the marketability. Once the Preliminary Title Report is complete, and title is cleared, the property is then sold. The volume of these title reports and property sales is the largest we've seen in our company's history."

Three areas which are expected to be of focus for our insiders in 2017 are technology, eClosings and marketing to consumers.

## Technology

The adoption and use of technology always has been a priority for Fortune Title, according to Plath. The agency is paperless.

"We take advantage of all technology that is going to benefit the company and the consumer as often as we can," she said. "We're always looking at new and inventive ways to gain efficiencies or make things easier at the closing table."

In an ideal world, Plath said, the industry would be paperless; closing packages would be delivered three days before closing, not just the Closing Disclosure; and the consumer would be more informed.



"(eClosing is) something everybody wants to do, but where is it on the priority list? Your first priority has to be compliance with all the rules and regulations."

**Nicole Plath,**  
CEO, Fortune Title

"I'd like to see documents that are interactive and explain to consumers what they are and what the terminology means, so they have a full understanding of what they're reading," she said.

That dream is not as far away as you may think, according to Fidelity Vice President of Information Technology, Agency Operations **Rick Diamond**. He said there haven't been any leaps forward, only baby steps so far. But, the industry is making progress.

"The ultimate goal is full integrations. Everything has to be integrated," Diamond said. "We've left behind the standalone process. I don't think there's any more of that in place, where you really have everything on paper. Not everything is integrated as of yet, but the standalone process I think is dead."

Last year portals were introduced to the industry. Regulations forced the industry to embrace a secure transfer of information and documents.

"What we're ultimately trying to get to is a secure portal for all data and all documents from the beginning of the transaction to closing," Diamond said.

Although the industry isn't there yet, Diamond said

it's slowly on its way. O'Donnell agreed. She said members of the industry have seen the rapid adoption of technology in their personal lives and the need to apply it to industry processes.

"I think the industry has a better recognition as a whole on what the future of the market looks like and who are the future purchasers," O'Donnell said. "The data will show you 30 percent of all purchasers are millennials at this point. How we're going to communicate and how we're going to close transactions for that group is going to be dramatically different."

These technical tools are important to the industry because of the efficiencies they bring, according to Diamond. "Ultimately it's going to save everybody time and money," he said. "Hopefully, that translates into more businesses for the agents and lenders. It keeps the process moving. The cost of these things should not be going up. They actually should be coming down. That's why we have to do this."

## eClosing

To maximize on the efficiencies of technology, the industry is beginning to adopt eClosings in a real way.

"I absolutely love eClosings," Plath said. "They streamline the process and make things much easier for the consumer. We've developed few relationships with banks that are doing eClosings in our area, but unfortunately most of them are not. We worked with one bank on an REO purchase and I called the mortgage broker to see if we could do more eClosings with them. They were surprised by our eagerness as they said most title companies don't want to participate in eClosings."

She said the benefit of eClosing is it streamlines the process. In New Jersey, Plath said eClosings have to be hybrids because a wet signature still is required on some documents.

"It's something everybody wants to do, but where is it on the priority list? Your first priority has to be compliance with all the rules and regulations," she said. "Until that's all ironed out and working smoothly, how can you take that next step into the eClosing?"

Westcor is making eClosing a priority for 2017.

"We're certainly looking into investing some time and money into what those transactions look like, looking into eClosing initiatives, looking at how we can use

technology to speed up the process," O'Donnell said. "We work collaboratively with our agents. We have several agents doing eClosing initiatives in conjunction with several of their customers — some cases large banks, some cases small community banks. We've been able to dedicate our IT resources and legal resources to work on title projects."

She said she wants to ensure Westcor's network of agents is well-positioned to transact in a paperless, eClosing environment.

"I think the laws are going to have to try and catch up a little. I think the secondary market wants to see eClosings and eNotarizations become more commonplace," she said.

## Consumer-direct marketing

A key benefit of eClosings is the increase in understanding by the consumer. With the Consumer Financial Protection Bureau putting emphasis on educating the consumer, the industry is considering the value of marketing directly to the consumer.

"We think our industry is recognizing the need to communicate directly with the consumer," O'Donnell said. "How people purchase is different and it's important for them to understand our industry better. I think it's going to be more and more a part of our world."

Plath said she has "dabbled" in consumer-direct marketing.

"We're vetting out a variety of social media companies for SEO optimization and getting placement on Realtor.com, Zillow or Trulia. We want to be seen where consumers are going before the house is purchased," she said. "It's more expensive than more traditional marketing methods, but we're entering an age where this is how people shop — they go online. We want them to know what title insurance is and how to choose their title provider before they sign a contract and possibly give that right to their attorney or realtor. This marketing strategy is a priority for us for 2017. We want to drive people to our website where they can see what we're about and we can cater to their needs."

## Looking ahead to 2017

Reaching out to consumers is not Plath's only goal for 2017. Aside from the desire to keep up 2016's momentum, she also wants to grow her staff, which has proven harder than she expected.

“It’s hard to find somebody to hire. In New Jersey attorneys used to do settlements as well as title agents. With all the new rules and regulations around settling a transaction, even just getting an attorney approved by some underwriters, has made it so that attorneys don’t want to be involved in that settlement anymore,” Plath said. “It’s put a lot of additional workflow on agencies who traditionally wouldn’t have done settlements. Consequently, it’s really hard to find experienced people. We’re now looking outside the real estate industry for people with the skills and abilities to do the job.”

Her concern for 2017 is that the industry will lose focus on American Land Title Association’s Best Practices, especially given the legal action against CFPB. Best Practices was a big focus, she says, but then it was moved to the back burner as everyone shifted focus to complying with TRID. However, Best Practices is an incredible tool, not only for satisfying a lender’s vendor management programs, but also for running a strong business.

Diamond said he expects the industry to make progress toward the adoption and utilization of technology.

“The industry is certainly moving towards more efficiency,” he said. “As time goes by, and as more integrations come into play in 2017, I think you’re going to see a lot more portals and a lot more integrations between the broker and the title agent, the title agent and the lender or the broker and the underwriter. With those in place you’re going to see

a lot more efficiencies.... My hope is this industry will adopt any technology that would help make it more efficient. Fidelity will continue to do everything possible to bring efficiencies to the process and make sure that we protect ourselves and protect our clients from a data security standpoint. Fidelity will be providing even more education to our agents as well as helping them in their back office procedures and using compliance and those efficiencies to promote new business.”

O’Donnell said Westcor will be looking at vendor management challenges for its customers. In 2017 the underwriter will be releasing software giving lenders the ability to manage their network of title agents more efficiently and in a web-based environment.

“We think the purchase market will continue to improve. We think prices will continue to improve,” she said. “I think you’ll see an equity market come back. We’re beginning to see signs of it.

“We’re excited about 2017. We think it’s a new chapter of aggressive growth for us.”

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## Liability, security to be focus in 2017

By Andrea Golby — Editor, *The Legal Description*

After a year of unexpected turns, following years of predictable scrutiny, legal issues title industry members will face in 2017 might seem like familiar territory. However, new developments may present new challenges to concerns industry members have become accustomed to addressing.

### CFPB bulletin and third-party oversight

In April 2012, the Consumer Financial Protection Bureau (CFPB) changed the relationship between lender and settlement service provider by releasing Bulletin 2012-03, putting lenders and service providers on notice that lenders will be held liable for the actions of their service providers. Four years

later, on Oct. 26, CFPB published a notice for a new bulletin in the *Federal Register*, which states, “The bureau is reissuing its guidance on service providers, formerly titled CFPB Bulletin 2012-03, Service Providers to clarify that the depth and formality of the risk management program for service providers may vary depending upon the service being performed — its size, scope, complexity, importance and potential for consumer harm — and the performance of the service provider in carrying out its activities in compliance with federal consumer financial laws and regulations. This amendment is needed to clarify that supervised entities have flexibility and to allow appropriate risk management.”

Although much of the language remains the same, it adds language stating, “The bureau expects that the depth and formality of the entity’s risk management program for service providers may vary depending upon the service being performed — its size, scope, complexity, importance and potential for consumer harm — and the performance of the service provider in carrying out its activities in compliance with federal consumer financial laws and regulations. While due diligence does not provide a shield against liability for actions by the service provider, it could help reduce the risk that the service provider will commit violations for which the supervised bank or nonbank may be liable, as discussed above.”

The addition of this language allows for some scalability for lenders and the title agents they work with, but questions remain about whether there is enough clarity for industry members to move forward with confidence.

“I think that is a really good step toward weighing the responsibilities of oversight against consumer choice in the selection of these service providers, because if there is no scalability, then I would say that the smaller title agencies are in peril because they won’t have the ability, infrastructure, or the money to achieve the level of compliance that the lenders are going to want in order to show the CFPB that they are overseeing their providers,” said **Roy Kaufmann**, of Counsel, Jackson & Campbell, P.C.

“Now mind you, one of the factors considered by the CFPB is the potential for consumer harm.” he continued. “That very broad factor may be an almost insurmountable. I think one of the tasks is to inform the CFPB, as long as the CFPB maintains its authority under president-elect Trump, that there has got to be consumer choice available in order for the industry to stay vibrant and as diverse as it is and as protective as it has been of the rights of the consumer.”

**Art Davis**, D.C. representative of the American Escrow Association (AEA), noted that under Section 1024(b)(2) of the Dodd Frank Wall Street Reform and Consumer Protection Act, the CFPB has supervisory authority over non-banks in the mortgage origination industry.

“As a service provider, what would make more sense to us is if they expand the supervisory examination manual, the closing section, which I don’t think they’ve done yet,” he said. “Then on top of that to put out materials that explain this stuff better. It’s not a matter of not wanting to be supervised or meet certain standards. Every member of AEA needs to be on the

right page of being compliant in all those areas and in keeping confidence of each and every lender they do business with. But I think it’s more helpful, once they decided to put that out there, to put more content in there about risk management because they already have it available to them in the statutory provisions in 1024(b)(2).”

**Nancy Silberberg**, president of Altus Escrow Inc. and president of the Escrow Institute of California (EIC), said the EIC is going to push for the definition of service provider to be changed in Dodd-Frank because it contends that industry members are service providers to the lender.

“We are hoping that through this new administration we can lessen the burdens that have been put upon our profession unjustifiably,” she said. “We do not provide material functions to the bank’s everyday process. They tie into our file. What I’m hoping for in this administration is that we can get some clarity; we can get some guidance. We can clarify the definition of service providers and we can possibly lessen some of the burden placed upon lenders because I don’t think it’s fair. I don’t think it’s appropriate that the lender has a right to become a de facto regulator of my company.

“So we want to clean that up,” she continued. “It will help the lenders as well. I’m not saying we shouldn’t do due diligence with the companies. In fact we do due diligence with the Realtors and the lenders to make sure they have the appropriate licenses. I think sometimes lenders go too far because they have no guidance from the bureau as to how far to go.”

## Cybersecurity

There was a lot of activity on the state and federal level regarding cybersecurity during 2016, and those efforts will continue into 2017.

“I think cybersecurity will be a big deal, but [we won’t know] until the administration changes,” said **Brian Thompson**, senior associate, Jackson & Campbell, P.C. and president-elect of the DC Land Title Association. “The election certainly drew a lot of attention to cybersecurity, so it was out there in the public, but how far they go with that and what they require [is unknown.]”

**Deborah Bailey**, partner, Gilroy Bailey Trumble, agreed.

“I think that cybersecurity will be a big issue this year,” she said. “We saw a lot of that even in the

# ATTENTION: **Attorneys**

A close-up photograph of a person's hand holding a white rectangular sign. The sign has the text "WE WANT YOU!" written on it. "WE WANT" is in black, and "YOU!" is in red. The background is a blurred image of a person in a dark suit jacket and white shirt.

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election itself. And I think we'll go back to basics and look at protecting the data because protection of the data we have is at the very heart of what we do. I'm not hopeful at the state level we will see a lot of action, but I think a lot of the changes that are made will come from the federal side."

Already, the Office of the Comptroller of the Currency, the *Federal Reserve* and the Federal Deposit Insurance Corp., published in the *Federal Register* an advanced notice of proposed rulemaking on enhanced cyber risk management standards. The proposed rulemaking is designed to "increase the operational resilience of a covered entity, lower the probability of a covered entity's failure or inability to serve as a financial intermediary and reduce the potential impact on the financial system of a cyber event affecting a covered entity."

"In response to the expanding cyber risks, the agencies are considering establishing enhanced standards for the largest and most interconnected entities under their supervision," the OCC wrote in a bulletin on the ANPR. "A covered entity is required to ensure that the services it receives from a third party are conducted consistent with the same standards that would apply if the covered entity conducted the operations itself. Thus, the enhanced standards would apply to all the operations of a covered entity regardless of whether the covered entity conducts an operation itself or through a third party." Comments to the rule are due by Jan. 17, 2017.

On a state level, in September, New York Gov. **Andrew Cuomo** announced a first-in-the-nation regulation had been proposed to protect New York State from the ever-growing threat of cyberattacks. The regulation requires regulated financial institutions to establish a cybersecurity program; adopt a written cybersecurity policy; designate a chief information security officer responsible for implementing, overseeing and enforcing its new program and policy; and have policies and procedures designed to ensure the security of information systems and nonpublic information accessible to, or held by, third parties, along with a variety of other requirements to protect the confidentiality, integrity and availability of information systems.

Several industry associations provided comments about the rule. Among other things the associations noted was that there has been a proliferation of cybersecurity regulations from multiple regulators at the state and federal level.

"We re-affirm our belief that any final rule would be

better served by careful coordination with existing cybersecurity regulations and requirements," a letter signed by the American Land Title Association, Mortgage Bankers Association, American Bankers Association, Financial Services Roundtable, American Financial Services Association, New York Mortgage Bankers Association, Financial Services Sector Coordinating Council and the Securities Industry and Financial Markets Association stated. "In addition to NIST's Cybersecurity Framework discussed above, FFIEC is vested with the power to develop uniform guidance and has separately promulgated the CAT to guide regulators and industry alike in maintaining comprehensive cybersecurity protections at financial firms. FFIEC also has developed comprehensive guidelines, such as the IT Examination Handbook, which consists of detailed guidance on cybersecurity protections. Regulations have also been issued in accordance with the GLBA. These regulations set uniform requirements for the entities regulated by the SEC, FDIC, Fed, OCC and other agencies with respect to the development and maintenance of a comprehensive information security program. At the international level, G-7 nations developed and released a set of voluntary guidelines for the financial sector. And just last month, the OCC, Fed and FDIC proposed enhanced cybersecurity requirements for large financial institutions and other firms."

Silberberg noted that it can be a challenge to draft legislation around these topics because it is an area that is constantly evolving and fluid. Regulators, legislators and the companies they govern have to continually be evolving as well.

"You have to be very diligent," she said. "I think businesses that have personal data information and money have to be extremely diligent in the coming years because the type and ferocity of the threats are going to get worse before it gets better. The threats will never stop, but I believe in time our industry will become more advanced on identifying the threats and avoid being compromised."

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# With *PHH Corp.* not finalized, industry hangs in the balance

By Katherine Bercik — Editor, *RESPA News*

On Oct. 11, 2016, the D.C. Circuit Court of Appeals handed down its decision in perhaps the most critical case involving the Consumer Financial Protection Bureau (CFPB) and RESPA since the bureau opened its doors in July 2011. In *PHH Corp. v. CFPB*, the court upheld a long-standing interpretation of RESPA Section 8 – that Section 8(c)(2) provides certain exemptions to Section 8(a)'s anti-kickback provisions – and determined that the CFPB's single-director, removable "for cause" only structure was unconstitutional.

As promised, the CFPB, on Nov. 18, filed a petition for rehearing *en banc*, asking for the full 11-judge D.C. Circuit panel to review the case. In its petition, the CFPB opposed the three-judge panel's findings on the constitutional question as well as its interpretation of RESPA. If the D.C. Circuit grants the petition for rehearing, then the initial opinion is vacated. At this point, it is just stayed.

On the eve of Thanksgiving Day, the D.C. Circuit issued an order asking for PHH Corp. to respond to the CFPB's petition. The order also invites the Solicitor General to weigh in on the petition for rehearing. This is a strong indication that the hearing *en banc* will be granted.

What does all of this mean for those wishing to utilize marketing services agreements (MSAs)?

In 2015, Wells Fargo, Prospect Mortgage and Bank of America announced that they would be discontinuing their MSAs. Earlier this year, in August, Colorado became the first state to officially ban MSAs. The D.C. Circuit's decision seemed to breathe new life into MSAs because it provided an exemption under 8(c)(2) for services rendered and goods provided. However, now with the CFPB's petition for rehearing on the RESPA issue, the CFPB has signaled that it plans to fight for its interpretation.

In prepared remarks at the Mortgage Bankers Association annual conference and expo in October, CFPB Director **Richard Cordray** reiterated that the bureau continues to adhere to the guidance bulletin it released in 2015.

Within the bulletin the CFPB outlined how it determines whether an MSA has violated Section 8 of RESPA: "In the bureau's experience, determining whether an MSA violates RESPA requires a review

of the facts and circumstances surrounding the creation of each agreement and its implementation. The nature of this fact-intensive inquiry means that, while some guidance may be found in the bureau's previous public actions, the outcome of one matter is not necessarily dispositive to the outcome of another. Nevertheless, any agreement that entails exchanging a Thing of value for referrals of settlement service business involving a federally related mortgage loan likely violates RESPA, whether or not an MSA or some related arrangement is part of the transaction."

If the D.C. Circuit grants *en banc* review, it will likely take another nine to 12 months before the full panel renders a decision (the cases will have to be briefed again and oral arguments will be held). The parts of the petition that get accepted for review will vacate the D.C. Circuit initially findings. Even if the D.C. Circuit does not accept the petition, there is still the option for the CFPB to appeal to the U.S. Supreme Court, as long as the U.S. Attorney General concurs with the CFPB's request, pursuant to 12 U.S.C. § 5564(e).

President-elect **Donald Trump** has nominated Sen. **Jeff Sessions** (R-Ala.) to be U.S. Attorney General. This means that there likely will be months or even years before this case and its implications for RESPA are finalized.

"Given the CFPB's appeal and the arguments that they're making before the *en banc* court, they seem to be sticking to their guns," Mayer Brown's **Phillip Schulman** told *RESPA News*. "So while I think there may be renewed interest [in MSAs], I think many companies will stay on the sideline, waiting to see how this appeal shakes out."

**Robert S. Niemi**, senior advisor at BakerHostetler, agrees that the CFPB has signaled to the industry that it still has grave concerns about MSAs. As of now, the CFPB's stance remains unchanged and while the bureau may not be so inclined to issue more RESPA enforcement actions in the near future, it retains its current supervisory and investigative authority.

"I think the only thing the *PHH* case settled so far is that firms don't have to worry about going back to three years before CFPB had enforcement ability under RESPA Section 8," Niemi told *RESPA News*. "If they are going to change the interpretation for what

you can and can't do, that's still going to be the same direction moving forward.

"It is a forward looking concern, not backward," Niemi added. "It doesn't change what companies need to be worried about or what companies need to monitor – what their originators are doing, what their sales offices are doing, what their companies are doing to partner with realtors to lease space, rent desks and to otherwise try to earn business from different third-party referral sources. Those microscopes are still out there."

So, what should you consider if you decide to continue utilizing MSAs?

**Ken Trepeta**, executive director and president of RESPRO, told *RESPA News* that he reverts back to a "Dos and Don'ts" pamphlet that the National Association of Realtors issued in 2014, while Trepeta was NAR's real estate services unit director.

Among that pamphlet's "Dos" are the following recommendations:

- Be aware that RESPA permits payments for services performed by a broker or agent only if actual services are performed and the fee is fair market value for the services performed.
- Memorialize an MSA in a written agreement that states in detail that marketing and advertising services to be performed and the fee to be paid in return for such services.
- Ensure that marketing and advertising services identified in a written MSA are actually performed.
- Consider incorporating a reporting or audit obligation in the written MSA that requires the service provider to document or otherwise provide evidence that services were performed.
- Provide disclosures to consumers notifying them of the MSA relationship.
- Document how the parties arrived at the amount of the marketing fee and the fair market value (it is also recommended to engage an independent third party to establish the fair market value of the marketing and advertising services).
- Be aware of the need to modify the amount, but only when objective changes are made to the services performed or to other terms of the agreement (always

verify the basis for the changes).

The pamphlet also includes a list of what you should not do while creating your MSAs:

- Do not include "services" in the MSA that require a broker or agent to market a lender or title company directly to a consumer (this includes sales pitches to a consumer or distributing lender or title company brochures directly to a consumer).
- Do not designate a settlement service provider as the broker or agent's "preferred" company as part of the MSA.
- Do not enter into exclusive MSAs such that the broker agrees to perform marketing and advertising services for only one lender or title company.
- Do not accept fees that are in excess of the fair market value of the marketing services actually performed.
- Do not base the amount of marketing fees on the volume of referrals or success of the referrals.
  - Do not accept fees under an MSA for allowing access to sales meetings, conducting consumer surveys or creating monthly reports.
  - Do not make frequent changes to the fees paid under an MSA based on the volume or success of referrals or any other non-objective criteria.
  - Do not enter into an MSA with a company that is an affiliate of the broker or agent.
  - Do not enter into an MSA with a month-to-month term.

"I think the only thing the PHH case settled so far is that firms don't have to worry about going back to three years before CFPB had enforcement ability under RESPA Section 8."

**Robert S. Niemi,**  
Senior Advisor, BakerHostetler

This is not an all-inclusive list.

"I've always been on the opinion that there is a right way and a wrong way to do an MSA," Trepeta said, adding that NAR had tried to get the CFPB to confirm this list of "Dos and Don'ts" but that the bureau instead maintained its stance that it was unsure that it is possible to create a proper MSA.

Also hanging in the air with *PHH Corp.* is the question of the CFPB's structure.

The D.C. Circuit struck out the Dodd-Frank Act's language stating that the director was removable for cause only, instead making the director removable at the president's will. However, until the CFPB's appeal is complete, the director can still only be removable for cause.

"So when President Trump comes into office, he

cannot remove the director,” Schulman said. “On the other hand, if Congress amended the statute before the *en banc* review is completed, by creating a commission or making the CFPB an executive agency, then the director could be removed. It’s unlikely, however, that Congress is going to act quickly on restructuring the CFPB. They have many other issues on their plate.”

Cordray’s term as director expires in 2018, however. Schulman added that it is possible that his term will expire before the case ultimately is concluded, especially if it is appealed and accepted for review by the Supreme Court.

In the meantime, the CFPB’s RESPA enforcement actions may be tempered. However, Niemi stated that there have been discussions within the industry of the possibility of a RESPA enforcement action being taken against a real estate agent.

“Whether that’s true, whether it’s going to work its way through, that’s a big question,” Niemi said. “We’ve heard about it for so long. Is it truly going to happen? ... Will there be fair enforcement of this act or will they just be going after lenders?”

## What else should the settlement services industry keep its eye out for?

Aside from the questions regarding RESPA, the CFPB and the outcome of *PHH Corp.*, the mortgage industry will face other major decisions within the next several months.

## Will regulations help or hinder appraisal profession?

By Mike Holzheimer — Editor, *Valuation Review*

Most people say they eagerly look forward to the future. Be it for personal or professional reasons, most look towards tomorrow as the start of something big. Still, a look ahead can be somewhat scary in that the unknown is a topic of conversation that provides very few answers as to job and financial security.

In the appraisal profession, there really isn’t a fear as to what is not known rather it is a frustration as to what has always been and what seemingly never will change. Appraisers have made it clear that guidelines and mistakes made in the past restrict the real estate evaluator of today prohibiting the promise of better and more profitable days ahead.

Where will the appraisal profession be in the next

On the mortgage licensing side, regulators currently are reworking and upgrading the licensing system.

How that’s going to roll out remains to be seen, Niemi said, adding that there will be many challenges facing companies that operate on a multistate level. That is because states still maintain their own mortgage licensing regulations, which may be more stringent than federal laws and regulations. The compliance gaps among states only create more challenges and confusion.

Another area of the mortgage sector that will experience a sweeping change will be those required to implement the new data collection requirements under the revised Home Mortgage Disclosure Act (HMDA). On Oct. 15, 2015, mere weeks after the TILA/RESPA Integrated Disclosure (TRID) rule became effective, the CFPB released its final HMDA rule, which expanded the data fields to be collected.

Two other areas of focus that Niemi discussed were the areas of data security and Section 342 of the Dodd-Frank Act.

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five years? Is there a light at the end of that proverbial dark tunnel regarding valuation? Are there legitimate and validated reasons for confidence and optimism amongst those in the profession or those about to choose such a professional career path?

*Valuation Review* had the opportunity to speak to some of the top professionals within the industry for their thoughts and concerns, as well as having the opportunity to play the role of fortune teller. The role of AMCs and lenders, through the eyes of the appraiser, shows a pattern of interference in their restraints and restrictions. The priority surrounding appraisers completing their assignments compliantly seemingly has been replaced by how

quickly an appraisal can be done with the least amount of expense involved. Simply put, appraisers feel as though there is a quantity over quality mentality, and they don't like it.

*Valuation Review's* 2016 Voice of the Appraiser survey spoke in part to the strained working relationships between appraisers, AMCs and lenders. And a more soothing, understanding atmosphere doesn't seem to be on the horizon. The majority of appraisers polled say regulations and third-party inclusions from the Home Value Code of Conduct (HVCC) and the Dodd-Frank Act are continuing to harm the appraisal profession.

"My greatest concern is not that the fees are low, but that lenders and AMCs continue to demand more and more detailed explanation without compensation for the added time and effort," one respondent said. "A lack of client loyalty is also a big concern. Even if you give the client the best appraisal ever at an incredible speed, they will pass you by on the next assignment because they found a fee somewhere for \$10 less. Why try to do your best if nobody cares and you are not rewarded?"

Appraisers also have adopted the belief that many AMCs have become advocates for the lender rather than managing the overall process. AMCs also may be turning into an enforcer for the lender, they say.

"The real estate valuation profession in the United States continues to evolve and advance, and – as has always been the case – appraisers who stay abreast of emerging trends will best be able to meet their clients' needs," Appraisal Institute President Scott Robinson said. "The number of appraisers likely will continue to shrink due to retirements, fewer new people entering the profession, economic factors, government regulation and greater use of data analysis technologies.

"Appraisal Institute research indicates that the number of licensed U.S. appraisers will continue to shrink at a rate that could match or exceed the current 3 percent decrease each year," Robinson added. "The number of licensed U.S. appraisers has shrunk more than 20 percent since 2007, according to Appraisal Institute research. That contraction of the valuation profession will provide opportunities for appraisers who remain current in their knowledge, expand their capabilities and best position themselves to respond to changing market demand."

The Appraisal Foundation's President **David S. Bunton** also said appraisers who remain on top of industry trends will be vital for the future.

"Appraisals performed by ethical and competent appraisers are a cornerstone of important decisions made for lending, litigation or other business purposes," Bunton said. "Although there are obviously fluctuations (e.g., 'bubbles') from time to time, the long-term trend for real estate in this country is clearly one of appreciation. It could be argued that in the years ahead, professional valuations will be even more important than they are today. However, appraisers will need to embrace new paradigms with respect to the roles they play.

"With the advent of 'big data' and evolving technology, there are those who believe a computer can provide a more 'accurate' opinion of value than appraisers," Bunton added. "There are many markets consisting of properties with varying ages, qualities of construction, condition, levels of renovation, lot sizes, view amenities, etc. — not to mention special financing arrangements or seller concessions. It is in these markets where a professional appraiser is needed to apply the type of judgment that a computer cannot replicate. While a computer can do a great job of 'crunching' numbers, its output is only as good as its input."

Bunton also said that appraisers are poised to be part of the solution.

"While the type and extent of analyses appraisers will perform is likely to be different than what has been done in the past, seasoned appraisers are some of the best candidates to accurately analyze and interpret market data. Indeed, financial transactions in the 21st century will be different. And professional appraisers are up to the challenge of meeting the needs of the marketplace," he said.

Periods of transition and adaptation also will be a part of future challenges for the appraiser.

"The appraisal profession, particularly as it pertains to the valuation of residential property, is going through a significant transition. It has its roots in the 1980s as we recovered from a major mortgage crisis prompted by extremely high interest rates," Columbia Institute Founder **George Harrison** said. "We saw the demise of the savings and loan industry, and residential lending being taken over by big, national lenders. To many stakeholders' amazement — including the local appraisers — mortgage lending became national rather than local.

"As the lenders 'left town,' the appraisers stayed. It was then necessary to adjust to this shift," Harrison added. "Local lenders typically had an appraiser or two either on staff or as a regular consultant/

contractor. This model worked well all the way around, but it was no longer feasible. To fill this gap, lenders resorted to the use of local mortgage brokers who would put the loan ‘package’ together. This included selecting the appraiser and ordering the appraisal. In essence, the new system was placing appraisal quality control in the hands of the broker (and/or underwriter).”

Harrison also mentioned five facts he sees occurring within the appraisal profession in the next five years:

- There will be a few, large AMCs;
- They will recruit new, younger appraiser trainees;
- They will provide training programs for their trainees;
- There will be opportunities for appraisers to advance within the profession; and
- There will be changes in the way appraisals are conducted and reported.

“These changes will see the URAR become obsolete,” Harrison said. “The form is already obsolescent in that it has to be modified and amended to meet current requirements, particularly as pertains to condition and quality of construction; and addenda to show analytics. We are already seeing the stakeholders, such as the large AMCs and firms, lenders and software vendors meeting to develop alternative reporting procedures that would be amenable to the secondary market lenders.”

Analytics will be a much bigger factor for appraisers going forward, William Fall Group CEO **William Fall** said.

“I believe the implementation of analytics will be much more in place than seen today,” he said. “Substantive defensible information contained within reports. Deeper discussion of meaningful market influences and their accompanying influence on value.

“Unfortunately appraisers remain viewed as another step to take in the approval of a loan,” Fall added, “often a stumbling block to getting the deal done. We need to convert that thinking to one that respects the independent judgment by a true professional that is independent of the transaction. Appraisers are overwhelmed today. Obviously compliance and diligence are closely tied. Individual appraisers will continue to be challenged to keep up.”

Fall suggested a few changes for the future to promote and enhance enthusiasm within the profession.

“I am encouraged by the recent activities of the

AQB (Appraiser Qualifications Board),” he said. “Honestly, and with future vision in mind, they are grappling with true solutions of how to increase participation in the profession without compromising competency. I look forward to specifics that will place more options for entry into the business, along with correlated education and supervision programs that have advancement responsibility in a properly monitored environment.”

CoreLogic Senior Vice President of Strategic Initiatives and Chief Appraiser **Jordan Petkovski** said the professional is in a “long overdue evolutionary process” that is driven by technology.

“In the future, residential appraisers will no longer spend their time on data acquisition in the traditional sense, nor will they be tethered to filling out forms. Instead, they will be more like micro-market economists, empowered with integrated data services and analytics suites,” he said. “They won’t just come up with a value but will be capable of efficiently providing their clients with objectively substantiated conclusions regarding value potential and underlying collateral risks.”

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**Jordan Petkovski,**  
Chief Appraiser, CoreLogic

# Industry's focus is squarely on Washington

By Chris Freeman — *Editorial Director*

Looking ahead from 2015 to 2016, lenders and bankers were focused on implementation of the TILA-RESPA Integrated Disclosure rule, the Home Mortgage Disclosure Act final rule, enforcement actions and regulatory compliance issues that may come up along the way.

The lending and banking world heading into 2017 is a very different place.

The surprising results of the elections have brought an element of uncertainty to the industry, combined with a feeling of potential improvements with Republicans in control of both houses of Congress and the White House. “Immediately after the election, many people around the industry said, ‘This is it. We can repeal this and repeal that.’ That was almost certainly over the top. Now, people are coming back down to the idea that we’re living in a world of practicality. What can we achieve to make the system work better?” asked one financial services industry insider.

The starting point for much of the federal legislative work that will affect the industry will be the Financial Choice Act that was offered in the summer by Financial Services Committee Chairman **Job Hensarling** (R-Texas). The sweeping bill brought Republican reforms to the Dodd-Frank Act in a variety of ways, from changing the structure of the Consumer Financial Protection Bureau (CFPB) to altering the way the Financial Stability Oversight Council designates systemically financial institutions, to repealing the Durbin Amendment and changing the scope of regulations being implemented by the Securities and Exchange Council.

The bill was dead in the Senate but now is looked at as the framework for starting Republican reforms, if not repeals, of the Dodd-Frank Act.

“Now Chairman Hensarling’s act is the floor,” Consumer Bankers Association President and CEO **Richard Hunt** said. “That’s repealing Durbin, and not only a commission for the CFPB but for FHFA

(Federal Housing Finance Agency) and the OCC (Office of the Comptroller of the Currency), too.”

In a speech before the Exchequer Club a week after the elections, Hensarling detailed his path forward and the way Republicans looked at their opportunity to overhaul the Dodd-Frank Act.

“The Founders believed ‘We the People’ were capable of governing ourselves. They distrusted unchecked power, so they limited government and promoted individual freedom, free enterprise and the rule of law,” he said. “These principles are what enable equal opportunity, prosperity and civil society to flourish. And on the Financial Services Committee, these principles are embodied in the proposals we offer.”



“I’m wary of the term deregulation. Regulation is important to the industry as long as it’s responsible.”

**Richard Hunt,**  
President and CEO,  
Consumer Bankers Association

Although Hensarling’s bill does not call for the repeal of regulatory bodies, he made it clear that the goal was to stop the threat to business and consumers he believes agencies have presented. He called it the rise of the fourth branch of government – agency government.

“Regrettably, when Americans look at Washington today, they see our federal government has drifted far from the Founders’ vision. Instead of limited government comprised of three accountable branches, they see power concentrated into a large and intrusive centralized government, ruled not by ‘We the People’ but by so-called experts in a new fourth branch that reaches further and deeper into our lives and tries to make decisions for us,” he said. “The rise of this fourth branch of government should concern every American. Because the rise of agency government risks turning our elections into a hollow exercise.”

Still, Hunt said the path forward in 2017 won’t be about rejection regulation, but about balancing it once again.

“I’m wary of the term deregulation. Regulation is important to the industry as long as it’s responsible,” he said. “It’s gone way too far on one end of the

spectrum, and we should try and bring a little balance in here. No one, including Speaker (**Paul**) **Ryan** and Chairman Hensarling, has called for the repeal of the CFPB or the elimination of the FDIC or OCC. There's a good, reasonable, balanced approach to regulation."

That should start, he said, with changes to the CFPB. Hensarling's bill calls for the bureau to become a bipartisan commission, to be subject to annual congressional appropriations rather than getting its funding directly from the Federal Reserve, and even to change its name to the Consumer Financial Opportunity Commission.

"Democrats who punted on the offer the industry made to have a five-person bipartisan commission, now I think they'll take that commission as a starting point," Hunt said. "The CFPB restructure has to happen."

Another major area to be addressed is reform for Fannie Mae and Freddie Mac. Treasury Secretary-nominee **Steve Mnuchin** already has said the priority is to privatize the government-sponsored entities (GSEs). That is a different tact than Hensarling's bill takes but with Sen. **Mike Crapo** (R-Idaho) set to retake the lead of the Senate Banking Committee, it could be in the works. Crapo helped co-author the last attempt at GSE reform in 2014.

Passing a reform bill in Congress is tricky, however, as GSE reform likely would raise mortgage fees and rates as the market prices in additional risk that the GSEs have been accepting up until now, on the behalf of the taxpayers.

But Mnuchin could enact some agency reforms on his own, with the Treasury Secretary in charge of the FHFA and its director, **Mel Watt**. Some of those could be changes to the joint stock agreement that has been in the works for the GSEs and Creighton said Mnuchin's background working at OneWest – the successor to failed lender IndyMac – shows he has the ability to get the job done.

"He did it. He didn't talk about it, he did it," the financial services industry insider said. "So when we look at the future, we have that background. ... I feel confident we have somebody capable if we have to solve a crisis, and that's a total good."

Two other areas that could be on the changed or repealed block are the Volcker Rule, which limits banks from proprietary trading in commodities and hedges, and the Durbin Amendment, which sets limits on the interchange rate charged by debit and credit card issuers to retailers.

On the Volcker Rule, Mnuchin discussed how a two-

sentence charge in the Dodd-Frank Act could spur a 900-plus page rule and his desire to cut back the rule itself and allow regulators to enforce the practice in the course of regular supervision.

The Durbin Amendment, meanwhile, would be repealed entirely, as its critics claim it is an example of the government stepping in to regulate rates in place of what had been a functioning market.

In his address to the Exchequer Club, Hensarling singled out two examples of regulatory overreach which Republicans would look to curb. The first is the Department of Labor's fiduciary rule, which he said would affect about \$3 trillion of retirement assets.

"It will make access to financial advice more costly and less available to millions of lower and middle income workers – and no one in Congress voted for it," he said.

"This is just one example of how unelected, unaccountable government hurts working people." Another example, he said, is the CFPB's small-dollar/payday lending proposed rule. The rule creates new restrictions and guidelines for lenders who issue small-dollar and payday loans and the CFPB itself has acknowledged that the rule could shutter between two-thirds and three-quarters of small businesses currently in the industry.

"These are just two examples of rule promulgated by the unelected and the unaccountable. These are just two rules that hurt struggling citizens. And these are two examples of rules the House Financial Services Committee, working with a President (**Donald**) **Trump**, hopes to reverse," Hensarling said.

How will the process work and how quickly can changes be made? That will depend on the willingness of leaders to work together on solutions.

"This is a prime opportunity for moderate Democrats in the Senate to work on bipartisan legislation," Hunt said. "Most of them are up for re-election in 2018. I don't think **Elizabeth Warren** is the future of the Democratic Party, so is there a place for moderate Democrats in the caucus?"

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