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Mortgage Disclosure Act And Multifamily Lending: Part 2

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Part one of this series offered an overview of how the amended Regulation C will impact multifamily housing under the Home Mortgage Disclosure Act, including which institutions and transactions are covered. Below we address reporting issues and challenges specific to multifamily housing.


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Applications and Multifamily Lending

HMDA's requirements are triggered when a financial institution receives an "application" for a covered loan. Current Regulation C defines the term "application" as "an oral or written request for a home purchase loan, a home improvement loan or a refinancing that is made in accordance with procedures used by a financial institution for the type of credit requested."[1] Amended Regulation C similarly defines the term as "an oral or written request for a covered loan that is made in accordance with procedures used by a financial institution for the type of credit requested."[2] In the preamble to the amended rule, the CFPB explains that Regulation C's definition of "application" is closely aligned with Regulation B's definition of the term[3] and "serves HMDA's fair lending purposes by requiring information about the disposition of credit requests ... that do not lead to originations."[4]

For consumer-purpose, one to four family residential mortgage loans, determining when a lender has received an application triggering HMDA's reporting requirements is fairly straightforward. For multifamily transactions, however, the issue is a bit more complicated because multifamily loans involve a "more fluid application process."[5] For example, a potential purchaser of a multifamily property might submit a pitch book request, i.e., investment package information specifying desirable loan terms, to one or more potential financing sources. Concerned about the complexities associated with applying HMDA to this type of scenario, commenters to the proposed Regulation C amendments asked the U.S. Consumer Financial Protection Bureau to exclude pitch book requests from the definition of the term application. The bureau declined this request, indicating that a uniform exclusion for pitch book requests could be problematic because institutions may not define and handle such requests consistently.

Although multifamily lenders will need to determine on a case-by-case basis whether pitch book requests or other interactions with potential multifamily borrowers are applications under HMDA,[6] the CFPB did offer some insight into how to analyze the issue. First, the bureau noted that the definitions of "application" in both Regulation B and Regulation C are flexible and closely related, and both regulations' official commentaries provide relevant guidance. In fact, the official commentary to Regulation C specifically states that "bureau interpretations that appear in the official commentary to Regulation B ... are generally applicable to the definition of application under Regulation C,"[7] except that the Regulation C definition of application does not include prequalification requests.[8]

Further, the bureau stated that, consistent with Regulation B's definition of the term "application," "[w]hether pitch book requests would be considered applications under Regulation C *would depend on how the specific financial institution treated such requests under its application process* ..."[9] The CFPB's official commentary to Regulation B similarly indicates that whether an inquiry about available loan terms becomes an application triggering the regulation's notification requirements "depends on *how the creditor responds* to the [applicant], not on what the [applicant] asks or says."[10] According to the official commentary, the following are examples of credit-related inquiries that are *not* applications:

- A potential borrower asks about loan terms and the lender explains its basic loan terms, such as interest rates, loan-to-value ratio (LTV) and debt-to-income ratio;
- A potential borrower asks about interest rates, the lender asks for down payment and collateral information and then communicates the rate;
- A potential borrower asks about loan terms and discloses his/her assets and income and intended down payment, and the lender explains its LTV and other basic lending policies without indicating whether the potential borrower would qualify; and
- A potential borrower asks about loan terms, discloses his/her income and the purchase price for the desired property and asks if he or she qualifies, and the lender responds by describing its general lending policies, explaining that it would need to review all of the potential borrower's qualifications before making a decision and offering to send the potential borrower an application.[11]

In other words, if a lender responds to an inquiry by commenting generally on available loan terms and required qualifications, but does not specifically communicate whether the potential borrower qualifies or not, the situation does not constitute an application under Regulation B. Applying this analysis to Regulation C, institutions receiving pitch book requests potentially could avoid treating such requests as applications triggering HMDA reporting by responding to such requests with information about their lending terms and criteria, but not commenting on whether the proposed transaction would qualify.

HMDA Reporting When Multiple Entities are Involved

In multifamily lending, as in other types of lending, it is common for more than one entity to be involved in the loan origination process. For example, a credit application may be evaluated by multiple creditors, by an institution that is providing contract underwriting services to a creditor or by an investor that

preunderwrites loans funded by a creditor from which it purchases closed transactions. In conjunction with its amendments to Regulation C, the CFPB expanded existing guidance and provided several examples regarding which entity has the responsibility to report a transaction when multiple entities are involved.[12]

CFPB Guidance Under Amended Regulation C

The general rule under the amended Regulation C is that the institution that makes the credit decision to approve or deny an application, or that was evaluating an application at the time that it was withdrawn or closed for incompleteness, is the entity that is responsible for reporting the transaction, even though that entity may not be the funding lender.[13]

If an institution approves an application based on underwriting criteria provided by a third party (such as Fannie Mae or Freddie Mac), and the third party did not review the application and did not make a credit decision on the application prior to closing, then the first institution is generally responsible for reporting the transaction.[14]

However, if more than one institution approved an application prior to closing, but only one of those institutions purchased the loan after closing, the institution that purchased the loan after closing generally reports the loan as an origination.[15]

An exception to the above rules arises if there is an agency relationship between two institutions. If an agent made the credit decision on an application on behalf of a principal, it is the principal that is responsible for reporting the transaction. According to the CFPB, "[s]tate law determines whether one party is the agent of another."[16] Although many contract underwriting relationships specifically disclaim any agency relationship between the parties, institutions should may still want to consider evaluating the features of such arrangements to ensure they do not qualify as agency relationships under applicable state law.

Examples of How to Report

The official commentary to the amended Regulation C provides a list of examples to help institutions understand how to report in complex situations:

[Investor Makes Credit Decision (Application Approved)] Financial Institution A received an application for a covered loan from an applicant and forwarded that application to Financial Institution B. Financial Institution B reviewed the application and approved the loan prior to closing. The loan closed in Financial Institution A's name. Financial Institution B purchased the loan from Financial Institution A after closing. Financial Institution B was not acting as Financial Institution A's agent. Since Financial Institution B made the credit decision prior to closing, Financial Institution B reports the transaction as an origination, not as a purchase. Financial Institution A does not report the transaction.

[Investor Makes Credit Decision (Application Denied or Withdrawn)] Financial Institution A received an application for a covered loan from an applicant and forwarded that application to Financial Institution B. Financial Institution B reviewed the application before the loan would have closed, but the application did not result in an origination because Financial Institution B denied the application. Financial Institution B was not acting as Financial Institution A's agent. Since Financial Institution B made the credit decision, Financial Institution B reports the application as a denial. Financial Institution A does not report the application. If, under the same facts, the application was withdrawn before Financial

Institution B made a credit decision, Financial Institution B would report the application as withdrawn and Financial Institution A would not report the application.

[Originator Makes Credit Decision and Sells Loan Post-Closing (Loan) Approved)] Financial Institution A received an application for a covered loan from an applicant and approved the application before closing the loan in its name. Financial Institution A was not acting as Financial Institution B's agent. Financial Institution B purchased the covered loan from Financial Institution A. Financial Institution B did not review the application before closing. Financial Institution A reports the loan as an origination. Financial Institution B reports the loan as a purchase.

[Originator Makes Credit Decision (Decline)] Financial Institution A received an application for a covered loan from an applicant. If approved, the loan would have closed in Financial Institution B's name. Financial Institution A denied the application without sending it to Financial Institution B for approval. Financial Institution A was not acting as Financial Institution B's agent. Since Financial Institution A made the credit decision before the loan would have closed, Financial Institution A reports the application. Financial Institution B does not report the application.

[Originator Makes Credit Decision Using Investor Guidelines] Financial Institution A reviewed an application and made the credit decision to approve a covered loan using the underwriting criteria provided by a third party (e.g., another financial institution, Fannie Mae or Freddie Mac). The third party did not review the application and did not make a credit decision prior to closing. Financial Institution A was not acting as the third party's agent. Financial Institution A reports the application or origination. If the third party purchased the loan and is subject to Regulation C, the third party reports the loan as a purchase whether or not the third party reviewed the loan after closing. Assume the same facts, except that Financial Institution A approved the application and the applicant chose not to accept the loan from Financial Institution A. Financial Institution A reports the application as approved but not accepted and the third party, assuming the third party is subject to Regulation C, does not report the application.

[Originator Makes Credit Decision Using Insurer or Guarantor Guidelines] Financial Institution A reviewed and made the credit decision on an application based on the criteria of a third-party insurer or guarantor (for example, a government or private insurer or guarantor). Financial Institution A reports the action taken on the application.

[Credit Decision Made By Agent of Originator] Financial Institution A received an application for a covered loan and forwarded it to Financial Institutions B and C. Financial Institution A made a credit decision, acting as Financial Institution D's agent, and approved the application. The applicant did not accept the loan from Financial Institution D. Financial Institution D reports the application as approved but not accepted. Financial Institution A does not report the application. Financial Institution B made a credit decision, approving the application, the applicant accepted the offer of credit from Financial Institution B and credit was extended. Financial Institution B reports the origination. Financial Institution C made a credit decision and denied the application. Financial Institution C reports the application as denied.[17]

Credit Decisions Made by Institutions That are not Subject to HMDA

In the preamble to the amended regulation, the CFPB indicated that in some cases, loans originated pursuant to a state housing financing agency (HFA) program may not be reported because the HFA usually makes the credit decision but is not subject to HMDA reporting requirements. In response to this comment, the bureau acknowledged that “some applications and loans will not be reported ... if the

institution making the credit decision is not ... required to report HMDA data."[18] This comment may provide insight to institutions that make loans that are underwritten before closing by an investor that does not qualify as a financial institution for HMDA reporting purposes.

The rules on this topic are complex, however, and careful analysis of specific situations may be necessary.

Other Issues That May Arise When Collecting and Reporting Data

The CFPB's amendments to Regulation C will expand the types of data that financial institutions are expected to collect and report. A few issues are particularly relevant to multifamily housing.

First, there is a special reporting requirement starting in 2018 that applies only to multifamily lending, regarding affordable housing: "If the property securing the covered loan or, in the case of an application, proposed to secure the covered loan includes a multifamily dwelling, the number of individual dwelling units related to the property that are income-restricted pursuant to federal, state or local affordable housing programs" must be reported.[19] A "multifamily dwelling" is defined as "a dwelling, regardless of construction method, that contains five or more individual dwelling units."[20] The CFPB has provided a nonexhaustive list of examples of federal, state or local programs that would trigger this requirement.[21]

Second, the CFPB has excluded multifamily housing from certain reporting requirements that are not suited to the multifamily context. For example, there are exemptions for loans secured by multifamily dwellings from reporting debt-to-income ratios, manufactured housing information and applicant credit score, age, race, ethnicity and sex.[22]

Finally, the CFPB's amendments recognize that a single loan might be secured by multiple properties. The general rule is that, when Regulation C calls for property-specific data such as the property address, the institution should choose one of the properties and report its address in the entry for that transaction.[23]

Amended Regulation C raises many challenging compliance questions for institutions making multifamily loans. Because both multifamily lending and HMDA compliance are an area of focus for the CFPB and other regulators, institutions making multifamily loans should consider evaluating their HMDA reporting processes for compliance with existing Regulation C and for future compliance with amended Regulation C.

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[1] 12 C.F.R. § 1003.2.

[2] 80 Fed. Reg. at 66,308 (to be codified at 12 C.F.R. pt. 1003.2(b)-1) (effective Jan. 1, 2018).

[3] Under Regulation B, an application "means an oral or written request for an extension of credit that is made in accordance with procedures used by a creditor for the type of credit requested. The term application does not include the use of an account or line of credit to obtain an amount of credit that is within a previously established credit limit." 12 C.F.R. § 1002.2(f).

[4] 80 Fed. Reg. at 66,138 (preamble).

[5] Id.

[6] 80 Fed. Reg. at 66,138 (preamble).

[7] 80 Fed. Reg. at 66,317 (to be codified at 12 C.F.R. pt. 1003, supp. I, comment 2(b)-1) (effective Jan. 1, 2018).

[8] Commentary to Regulation B states that "a creditor is encouraged to provide consumers with information about loan terms [but] if in giving information to the consumer the creditor also evaluates information about the consumer, decides to decline the request, and communicates this to the consumer, the creditor has treated the inquiry or prequalification request as an application . . ." 12 C.F.R. pt. 1002, supp. I, comment 2(f)-3.

[9] 80 Fed. Reg. at 66,138 (preamble) (emphasis added).

[10] 12 C.F.R. pt. 1002, supp. I, comment 2(f)-3 (emphasis added).

[11] 12 C.F.R. pt. 1002, supp. I, comment 2(f)-4.

[12] The current guidance is at 12 C.F.R. pt. 1002, supp. I, comments 1(c)-2, 1(c)(3). The revised guidance is located at 80 Fed. Reg. at 66,322-33 (to be codified at 12 C.F.R. pt. 1003, supp. I, comments 4(a)-2, 4(a)-3, 4(a)-4) (effective Jan. 1, 2018).

[13] Id.

[14] 80 Fed. Reg. at 66,323 (to be codified at 12 C.F.R. pt. 1003, supp. I, comment 4(a)-3(v)) (effective Jan. 1, 2018).

[15] 80 Fed. Reg. at 66,322 (to be codified at 12 C.F.R. pt. 1003, supp. I, comment 4(a)-2(i)) (effective Jan. 1, 2018).

[16] 80 Fed. Reg. at 66,323 (to be codified at 12 C.F.R. pt. 1003, supp. I, comment 4(a)-4) (effective Jan. 1, 2018).

[17] 80 Fed. Reg. at 66,322-33 (to be codified at 12 C.F.R. pt. 1003, supp. I, comment 4(a)-3) (effective Jan. 1, 2018).

[18] 80 Fed. Reg. at 66,173 (preamble).

[19] 80 Fed. Reg. at 66,311 (to be codified at 12 C.F.R. § 1003.4(a)(32))(effective Jan. 1, 2018).

[20] 80 Fed. Reg. at 66, 309 (to be codified at 12 C.F.R. § 1003.2(n)) (effective Jan. 1, 2018).

[21] 80 Fed. Reg. at 66,336 (to be codified at 12 C.F.R. pt. 1003, supp. I, comments 4(a)(32)-1, 4(a)(32)-2) (effective Jan. 1, 2018).

[22] See 80 Fed. Reg. at 66,308-20 (to be codified at 12 C.F.R. §§ 1003.2(b)(2), 1003.4(a)(10)(iii), 1003.4(23), 1003.4(29) and 12 C.F.R. pt. 1003, supp. I, comment 2(n)-2) (effective Jan. 1, 2018).

[23] See 80 Fed. Reg. at 66,327 (to be codified at 12 C.F.R. pt. 1003, supp. I, comments 4(a)(9)-2, 4(a)(9)-3) (effective Jan. 1, 2018).