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Not a Humdrum Affair: HMDA Changes and Controversies

Legal Update
09.03.2019

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The Consumer Financial Protection Bureau (CFPB) is considering two significant changes to Regulation C, the implementing regulation of the Home Mortgage Disclosure Act (together, HMDA), which could lighten the compliance burden on smaller banks. These proposed changes will impact both consumers and the community banking industry.

Data Point Collection

On May 8, 2019, the CFPB issued an Advance Notice of Proposed Rulemaking soliciting comments on whether to alter the data collected under HMDA. Currently, nonexempt institutions must report numerous data points on mortgage applications and loan originations, including age, race, and sex of the applicant, credit score, loan term, origination charges, and more. Based on the feedback received, the CFPB may change what data is collected and for what types of loans lenders must report that data.

Exemption Thresholds

On May 13, 2019, the CFPB issued a proposed rule affecting reporting exemption thresholds under HMDA, with an implementation date of January 1, 2020. Currently, an institution is exempt from reporting closed-end mortgages if it originated fewer than 25 in the past two years and is exempt from reporting open-end lines of credit if it originated fewer than 500 in the past two years. This latter threshold will be reduced to 100 lines of credit at the end of 2019. The proposed rule would institute the following changes to HMDA:

- Permanently raise the closed-end mortgage threshold to either 50 or 100 mortgages;
- Extend the open-end threshold of 500 lines of credit to the end of 2021; and
- Set the open-end threshold to 200 lines of credit starting in 2022.

Additionally, the proposed rule would provide guidance on, and make minor adjustments to, the current requirements for a partial exemption that allows institutions originating fewer than 500 mortgages to avoid reporting on some, but not all, HMDA data points.

Impacts – The Good

The decreased compliance burden resulting from these rule changes could translate into significant cost savings for some banks. As of 2015, according to the CFPB, financial institutions spent an annual aggregate amount of $489 million on software, staff, and other resources to comply with reporting obligations under HMDA. The CFPB estimates annual compliance costs range from $529,400 for institutions it classifies as "Tier 1 Institutions" (those reporting roughly 50,000 records annually), to $71,000 for "Tier 2 Institutions" (those reporting roughly 1,000 records annually), to $8,650 for "Tier 3 Institutions" (those reporting roughly 50 records annually). Closed-end mortgage reporting alone constitutes a significant chunk of these costs. If not partially exempt, the CFPB estimates annual costs of approximately $343,000 for Tier 1 Institutions, $44,700 for Tier 2, and $4,500 for Tier 3.

Cost savings from the new rule will vary. If the closed-end mortgage threshold is increased to 50, the CFPB estimates an aggregate annual savings of $2.2 million on operational costs among 760 newly-exempt institutions. If increased to 100, that estimate increases to $8.1 million among 1,718 newly-exempt institutions. The vast majority of newly-exempt institutions under the proposed rule are Tier 3 Institutions and thus could expect to save roughly $4,500 per year. A minority of newly-exempt institutions would be Tier 2 Institutions, which could save roughly $44,700 per year. These savings could vary, of course, given any one-time costs incurred in adapting to the new rule.

Impacts – The Controversial

The CFPB acknowledges that these proposals do have potential downsides, and critics agree. In June 2019, members of the Senate and the House of Representatives penned two separate letters to the CFPB, expressing concerns that the reduced data availability is contrary to HMDA's statutory purposes, ignores post-crisis safety and soundness concerns, and minimizes the value of consumer protection and fair lending.

Naturally, fewer reporting institutions will result in decreased available data on consumer lending practices – data upon which the regulators depend to monitor for discriminatory lending practices and Community Reinvestment Act (CRA) compliance. In 2017, roughly 7 million closed-end mortgages were reported under HMDA. The CFPB estimates that a closed-end threshold of 50 mortgages will result in 37,000 fewer mortgages reported; if the threshold is set to 100 mortgages, that number increases to 147,000 unreported mortgages.

While this may not seem like a dramatic decrease in data, concerns have been raised that the underreporting would particularly affect rural communities that are predominantly served by smaller banks which might slip under the new reporting threshold. A reduction in available data for such areas may obscure potential discriminatory lending practices and reduce insight into consumers' needs for mortgage credit. There is risk to the lenders too. As the proposed rule points out, insufficient HMDA data could lead to certain institutions being misidentified as high-risk for fair lending issues.

Conclusion

While the future of these proposals remains uncertain, these changes could certainly ease the compliance burden and cost on small and midsized banks. Whether lawmakers and regulators decide these benefits outweigh the potential impact on monitoring compliance with anti-discrimination laws remains to be seen.