

**REGULATION OF MORTGAGE LENDING  
IN NORTH CAROLINA:  
WHERE WE ARE AND WHERE WE ARE GOING**

Presented to the  
North Carolina Association of Mortgage Professionals  
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I am happy to be with you today and would like to thank you for the opportunity. I always look forward to meeting with industry groups so that I can let them know what my colleagues and I are up to and, more importantly, to listen to their points of view. This is particularly true with regard to the mortgage lending industry. As you may know, I am a “bank” guy who thought that being Commissioner of Banks meant what the title implied. I didn’t fully appreciate when I accepted Governor Easley’s appointment that I would also become a (or the) “Mortgage Czar.” That’s life I suppose; sometimes you get what you don’t expect or deserve. Let it suffice to say that the mortgage lending industry has become a bigger part of my life than I had anticipated. I hope that our time together today will be a mutual learning experience.

I would like to review with you three subjects that significantly affect the mortgage industry in North Carolina: (i) implementation of the Mortgage Lending Act; (ii) the current state of the mortgage market and its implications for enforcement activities by the Office of Commissioner of Banks (“OCOB”); and (iii) recent studies regarding the longer-term future of the industry.

### **Mortgage Lending Act Implementation**

As you know, the Mortgage Lending Act (the “MLA”) was enacted by the 2001 Session of the General Assembly, with an effective

date of July 1, 2002. The MLA was amended by the 2002 Session of the General Assembly to, among other things, permit the granting of “limited” or “exclusive” licenses to loan officers employed by large insurance or consumer finance firms. Implementation of MLA has taken a substantial amount of time and resources in the last year. While we have made progress, there is much more to do.

The first phase of MLA implementation has been the initial licensure of approximately 1,200 mortgage bankers and brokers and over 11,000 loan officers. This phase has involved development of an IT infrastructure capable of managing the licensing process and handling a huge flow of applications during a relatively short period of time. Because of these “first time” issues, our processing of applications was slower than I would have liked, with our “grandfathered” applications expected to be completed in March of this year. Our people worked very hard and did very well under somewhat adverse circumstances. Our goal is to handle new applications and renewals much more efficiently in the future.

Speaking of “grandfathered” applications, I would remind you that the “grandfathered” loan officers have an eight-hour continuing education requirement that has to be met before their licenses can be renewed. I am told that only 1,200 to 1,500 have satisfied that requirement to date. Do not let this catch you by surprise. There are

plenty of sources for this education, and I am pleased to see that a great deal of education will be accomplished at this meeting.

In addition, the Banking Commission has implemented temporary regulations under the MLA. The Commission also adopted final regulations, which were published and were the subject of public hearings under the North Carolina Administrative Procedure Act (NCAPA). These final regulations have been approved, with revisions, by the North Carolina Rules Review Commission. Given the further requirements of NCAPA, these regulations will not be effective until April of this year. Prior regulations will, of course, cease to be effective at that time.

The MLA contains a “grandfather” provision that requires licensure of covered personnel who were employed by firms in the business on July 1, 2002 and were registered with the OCOB. The grandfather provision also extends to persons who were employed by firms exempt from registration under prior law but who must now be licensed. “Grandfather” status is not extended to: (i) loan originators, generally employed by insurance or consumer finance companies, who are “limited loan officers” or “exclusive mortgage brokers” under revisions to MLA enacted by the General Assembly in 2002; and (ii) persons or entities who do not meet the statutory requirements for licensure for reasons such as prior criminal record or lack of financial responsibility.

To date, OCOB staff has approved “grandfathered” applications for 326 mortgage bankers, 475 brokers and over 9,000 loan officers. Staff has denied 467 applications for licensure. Approximately 1,800 applications are still under review or in process, the bulk of such remnant comprising “exclusive” or “limited” licenses.

A denied applicant has the right to appeal, first to the Commissioner, then to the Banking Commission, and finally to Wake County Superior Court. To date, I have heard or am scheduled to hear about 70 matters, with many more in process. While I have upheld denials in many cases, I have vacated denials and ordered the issuance of licenses as a result of a significant number of appeals. My colleagues and I have tried to be fair in our proceedings and are working to make the appeals system more efficient; however, the handling of appeals will be a major activity for us for the foreseeable future.

Denials of MLA applications are based on contravention of one or more provisions of N.C.G.S. §53-243.12. While each case is different, our experience to date has raised a number of issues regarding denials that I would like to take this opportunity to address. These issues are as follows:

1. Contravention of one or more of the provisions of N.C.G.S. §53-243.12 (*e.g.*, a criminal record, lack of financial responsibility) will cause an application to be held for further review. In the absence of a showing in the application or by subsequent additional information of countervailing factors in favor of the applicant, the application will be rejected. Presentation of favorable evidence in connection with an appeal can, and has, resulted in issuance of a license. To be successful, the applicant's evidence should be direct and extensive enough to overcome the factors that caused the initial rejection.
2. Applications for mortgage banker and mortgage broker licenses are held to a stricter standard of performance than applications to be a loan officer. A license to be a mortgage banker or broker requires the applicant to have the ability to manage the assets of clients and to supervise others. Loan officers, on the other hand, are subject to supervision and control.
3. Willful failure to disclose disqualifying information in an application creates a very strong presumption that the applicant should not be licensed. Negligent failure to do so raises a rebuttable presumption of incompetence on the part of the applicant.

4. In the case of “grandfathered” licenses, a letter denying licensure is not effective if the applicant timely makes an appeal. Denial is stayed pending final resolution of the appeal, whether at the Commissioner, Commission or court level. Denial letters are strongly worded because they are effective as of their date if the applicant does not appeal. In the case of new applications, of course, the applicant cannot transact business unless and until a license is issued.
5. Applicants represented by counsel have done much better in appeals proceedings under the Mortgage Lending Act than those representing themselves. While I cannot require an applicant to obtain counsel, or appoint one for applicants, it is my strong advice that applicants get competent counsel when and if their applications are denied or they are the subjects of administrative action by OCOB.

In sum, the denial and appeal processes are works in progress. My colleagues and I are mindful of the impact denial can have on the lives of applicants and their families. We are also mindful of the impact that dishonest or incompetent mortgage bankers, brokers and loan officers can have on their customers. We are doing the best we can to balance the equities involved in these matters.

## Next Steps

Once the initial MLA implementation has been completed, OCOB's next activities will be examination of mortgage firms and enforcement actions for violations of MLA and other North Carolina laws regarding retail mortgage lending (*e.g.*, the predatory lending law). OCOB has recently hired more investigators, so we have the resources to do the job; the key for us will be to concentrate our resources where they will do the most good.

I regret to say, I think we will have a significant number of targets for investigation. Of the 1,200 or so consumer complaints OCOB gets each year, approximately two-thirds relate to non-bank mortgage lenders. Accordingly, our first steps on the investigative front will be to organize and pursue complaints that we receive from the public. The recent upgrading of our IT infrastructure, mentioned earlier, will materially assist this process.

I am not an economist, but by virtue of my position I receive economic forecasts and assessments of economic and business conditions in North Carolina and the Southeast. While these forecasts aren't dire, they aren't particularly rosy either. As a veteran of the real estate troubles of the 1980s and 1990s, my tendency to pessimism is somewhat heightened at present. This feeling is shared by my

colleagues and, as a result, we are going to be on the lookout for abuses that result from a need for volume in a slow market: loan churning, appraisal inflation, fee gouging, property flipping. If and when we find this kind of conduct going on, please be assured we will act promptly and vigorously.

### **A Brief Look at the Long-Term**

As someone with a stake in the long-term health of the mortgage lending industry, I would like to suggest that it would be in your interest to address in a serious way issues of diversity and consumer protection if you have not already done so. This isn't merely a question of political expediency for your industry, although it is politically expedient. It is good business. Let me explain.

Harvard University's Joint Center for Housing Studies has recently issued a publication entitled The State of the Nation's Housing: 2002. This publication, which is available from the Joint Center's web site, is worth reading. Among other things, it points out that the demographic trends make it likely that the housing market of the future will be substantially different from the market to which all of us are accustomed. The study points out that:

Over the next 20 years the number of U.S. households will likely increase 22.6 percent to 129 million. Minorities will account for

almost two-thirds of this growth, climbing 59 percent to over 41 million households. At the same time the number of non-family households will most likely rise by 9.4 million (28 percent). By 2020 the 43 million non-family households will thus make up a third of all households.

These changes in the race, ethnicity, and family structure of households will substantially alter the characteristics of homeowners. After dominating the homebuyer market throughout the postwar period, white families will account for less than 30 percent of the 22.2 million net new homeowners added by 2020. The number of minority homeowners will increase by 10.4 million to 22.5 million over this period, lifting the minority share of all owners to 24 percent. Non-family homeowners will also increase in number by 7.8 million, or 45 percent.<sup>i</sup>

In light of the trends just cited, appreciation and acceptance of diversity aren't just politically correct, they are good (and perhaps necessary) business. Opening of access to these new homeowners will require a change in the way all of us do business.

The trends just cited also bring potential social and political difficulties for the mortgage industry. As you know, the MLA is a second and supplemental response to perceived abuses in the mortgage

market, primarily the subprime segment, that were initially addressed by North Carolina's predatory lending statute. While I appreciate the attitude that the industry has taken with regard to these legislative and regulatory efforts, I must tell you that the demands created by the demographic trends just discussed will create social and political pressure for growing access by the new homeowners to the mortgage market on a fair and equitable basis. This pressure can work itself out through the market accommodation or regulatory fiat (*a la* the Community Reinvestment Act that applies to regulated depository institutions). As your friend, I will tell you that a market-based resolution of this issue is better, but it won't just happen. Effective functioning of markets requires, among other things, relatively equal bargaining position, knowledge and information. If, as I do, you want a market-based response to the new demand, may I suggest that you have a big stake in enhancing our society's financial literacy.

The State Treasurer, who is chairman of the Banking Commission, has established financial literacy as one of his priorities for this year. It is one of my priorities also. This concern is shared by the Banking Commission members; and, as a result, I expect that we will embark on significant new financial literacy activities over the next several years. I hope we can count on the mortgage industry to participate with us in this effort, particularly in the area of home ownership counseling. I also hope that you will seriously consider supporting other efforts to enhance financial literacy, such as Camp

Challenge, a summer camp for at-risk youth that emphasizes financial literacy training.

## **Conclusion**

Thank you again for having me this afternoon. Your industry has done remarkable things to advance home ownership in the United States and looks to be poised to continue that activity in new and exciting ways in the future. I look forward to working with you to that end.

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<sup>i</sup> Joint Center for Housing Studies of Harvard University, “The State of the Nation’s Housing 2002”, p.12, at <http://www.jchs.harvard.edu/publications/markets/Son2002.pdf>