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New Fed rules aim to protect home buyers

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WASHINGTON • In a move long sought by consumer advocates, the Federal Reserve issued on Monday rules intended to prevent brokers and lenders from unfairly profiting from new mortgage loans.

The rules ban the abuse of the yield-spread premium, a practice that often put buyers into unstable and expensive loans simply to generate extra commissions.

"This is a real milestone," said Michael Calhoun of the Center for Responsible Lending, which had long argued against the premiums.

"People didn't just happen to end up in risky loans during the boom," Mr. Calhoun added. "Mortgage brokers and other people on the frontlines were getting two to three times as much money to push buyers into those loans than they were into 30-year fixed-rate loans. So what do you think happened?"

In some cases, borrowers never knew they were paying more in interest than they needed to. In others, they thought they were saving money by exchanging lower fees for a higher rate. But consumer groups argued that the borrowers often ended up paying both higher fees and a higher rate.

While the new rules prohibit payments to a lender or broker based on the loan's interest rate, they allow for compensation based on a fixed percentage of the loan amount.

The Fed rules take effect in April. Similar and in some ways more comprehensive rules are in the financial reform bill that passed Congress this summer. Those rules will take effect later.

Fannie Mae and Freddie Mac in spotlight • The administration of President Barack Obama will bring together bankers, investors, housing experts and policymakers today for the Conference on the Future of Housing Finance. The goal is to address the problems of Fannie Mae and Freddie Mac.

Practically all new U.S. mortgages are guaranteed by Fannie Mae and Freddie Mac and the Federal Housing Administration. Since the credit crisis began the Federal Reserve has purchased $1.1 trillion in agency mortgage securities as a means of propping up the market and keeping loan rates low. This creates great risk for the taxpayers.

Fannie Mae and Freddie Mac "are quite profoundly broken," economist Raj Date of the Cambridge Winter Center told CNN. "But no one wants to disrupt the only thing that's working right now in the mortgage market."

Congress under pressure • Rep. Barney Frank, D-Mass., said the House Financial Services Committee would hold hearings in September on the Fannie Mae and Freddie Mac situation.

Lawmakers agree that Fannie and Freddie should stop borrowing heavily from the capital markets. Beyond that, there is little agreement.

Democrats seem to be moving in the direction of turning Fannie and Freddie into much smaller entities that buy individual mortgages, pool them and sell them back into the market to private investors. Republicans who don't back a fully private market are likely to push for a government guarantee that is available for any corporate mortgage investor packaging loans, not just Fannie and Freddie.

However, some sort of government guarantee is likely, largely because of the influence of the housing lobby, including the Mortgage Bankers Association, the National Association of Realtors and the National Association of Home Builders.

"The housing industry is dead set on having guarantees," said Mark Calabria, of the CATO Institute in Washington.