

# MAINE STATE LEGISLATURE

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DEPARTMENT OF PROFESSIONAL AND FINANCIAL REGULATION

**BUREAU OF CONSUMER CREDIT PROTECTION**

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To: Jeffrey H. Butland, President, Maine State Senate  
Dan A. Gwadosky, Speaker, Maine House of Representatives  
From: Will N. Lund, Superintendent  
Bureau of Consumer Credit Protection  
Re: Report Pursuant to PL Chapter 268 (1993),  
"An Act Related to Mortgage Companies"  
Date: December 30, 1994

Enclosed please find a report detailing resource expenditures and revenue sources for the Bureau of Consumer Credit Protection, as requested by the Joint Standing Committee on Banking and Insurance in Section 3 of PL Chapter 268 (1993), "An Act Related to Mortgage Companies."

I am proud of the excellent work done by Bureau staff in assisting Maine consumers in their credit dealings with Maine mortgage companies, banks, credit unions, credit reporting agencies, collection agencies, loan brokers and retail creditors, and I look forward to the opportunity to personally present this information to the Committee.

WNL/bas  
ENCLOSURE

NOV 22 1996

Bureau of Consumer Credit Protection

Report to Joint Standing Committee  
on Banking & Insurance

Pursuant to PL Ch. 268 (1993)

"An Act Related to Mortgage Companies"

January 1, 1995

The Maine Bureau of Consumer Credit Protection (the "Bureau") is a 100% dedicated revenue account agency, which means that it receives no annual appropriation from the tax-supported General Fund. Rather, the agency's funding comes from a combination of volume fees, license fees, exam fees and investigative cost assessments charged to the companies it regulates. Regulated entities include mortgage companies, savings banks, commercial banks (trust companies), credit unions, general creditors (such as auto and appliance dealers), credit reporting agencies, debt collectors, repossession companies, loan brokers, pawnbrokers and rent-to-own companies.

In May of 1993, the Second Regular Session of the 116th Legislature passed L.D. 591, PL 268 (1993), "An Act Related to Mortgage Companies." This law amended the statutory funding formula for the Bureau in several ways:

- It retained the volume assessment for general creditors at the rate of \$25 per \$100,000 (or 25¢ per \$1000) of credit extended.
- It reduced the volume fees for banks and credit unions by 20%, from \$25 per \$100,000 to \$20 per \$100,000.
- It imposed a volume fee on mortgage company loans made at less than 12½% APR, at the reduced rate of \$20 per \$100,000, effective 1995.

Application of this new rate to mortgage companies, and the reduction of the existing rate with respect to banks, led to discussions during committee debate on the bill concerning apportionment of the income and expenses of the Bureau among the various companies regulated by the agency. For that reason, the Banking and Insurance Committee amended the bill to add a provision requesting a report from the Bureau, due January 1, 1995, discussing the sources of revenue for the agency and how those sources compare with the agency's expenditures.

This report, therefore, will describe the proportional amounts of time and revenue expended on the various categories of businesses regulated by the Bureau. It will compare these expenditures to the income derived from these businesses, and discuss options for further reapportionment of the agency's expenses.

## **2. Information Sources**

The Bureau maintains records of its sources of revenue in conformity with State audit standards (the most recent audit having occurred in 1993). Revenue from volume fees, examination

reimbursements, and fees for licenses and registrations are all recorded by specific source. This data is retrievable as part of the MFASIS state computer budgeting system.

With respect to expenses, Bureau employees conducted various studies in order to determine the sources of personnel costs to the agency. These included maintenance of telephone logs, time sheets by category of business addressed, incoming mail analysis and thorough review of examination practices by type of creditor. In addition, consumer complaints were analyzed for content and business type.

### 3. Summary of Findings

As detailed in the following pages, licensed supervised lenders (mortgage companies) and state-chartered financial institutions (including trust companies, savings banks and credit unions) are primary sources of funding for the Bureau through volume fees and examination reimbursements. They also extend the most credit to Maine consumers, and the loans tend to represent major purchases (residence, automobiles) for those consumers.

General creditors (merchants who sell on credit) contribute lesser amounts, although they reimburse the Bureau for all examination expenses, and actually pay volume fees at a 20% higher rate than mortgage companies and banks.

Collection agencies, credit reporting agencies and credit services organizations (loan brokers) reimburse the Bureau for compliance exams. They pay license or registration fees to cover the costs of processing initial and renewal applications. They do not, however, contribute to the general consumer complaint or regulatory overhead of the Bureau, because they are not subject to assessments that are the equivalent of volume fees paid by lenders and creditors.

While it is possible to amend Maine's laws to assess loan brokers, credit reporting agencies and collection agencies based on their volume of business, strong policy arguments exist that 1) creditors and lenders have benefitted from the Bureau's successful efforts to maintain firm regulation over those three "service" industries; 2) all three are already regulated more heavily in Maine than in almost any other state; and 3) the three industries, if required to pay volume fees, would simply pass those costs onto their customers, which are the lenders and creditors which employ them to assist in the application and collection procedures.

In addition, there exist large segments of expense for which the Bureau does not and cannot expect reimbursement or assessment of fees, but for which the agency is nonetheless expected to respond and provide expertise to various recipients. These include regulation of unlicensed lenders attempting to solicit businesses in Maine, out-of-state credit card issuers, unlicensed collection agencies and a myriad of credit related perpetrators of scams, against Maine citizens, via telephone and the mails. Having identified this segment as an unreimbursed expense, the Legislature must evaluate the extent to which Maine business should continue to fund an agency to which consumers can voice their complaints, questions and concerns and, if so, whether to continue the current means of funding the agency or determine other methods.

#### **4. Bureau's History**

Twenty years ago, consumer credit-related laws were a mix of small loan laws, usury limits and miscellaneous other provisions scattered throughout the Maine statutes. In 1975, the Maine Legislature created the Bureau of Consumer Credit Protection through passage of a version of the Uniform Consumer Credit Code ("the Code") which codified many existing laws, and provided many new consumer rights (e.g., a Notice of Right to Cure Default before fore-closure or repossession; a 3-day right to rescind a credit transaction in which a security interest was taken in a consumer's residence; etc.). Through the Code, Maine enacted Truth-in-Lending, so that Maine consumers would have remedies at the state level if a creditor failed to disclose the true cost or terms of a credit or loan transaction. Maine applied to the Board of Governors of the Federal Reserve ("the Board") and, based on the State's laws and the history of aggressive, knowledgeable enforcement of Truth-in-Lending principles by administrators and examiners at the Bureau, the Board granted Maine an exemption from federal jurisdiction in this area.

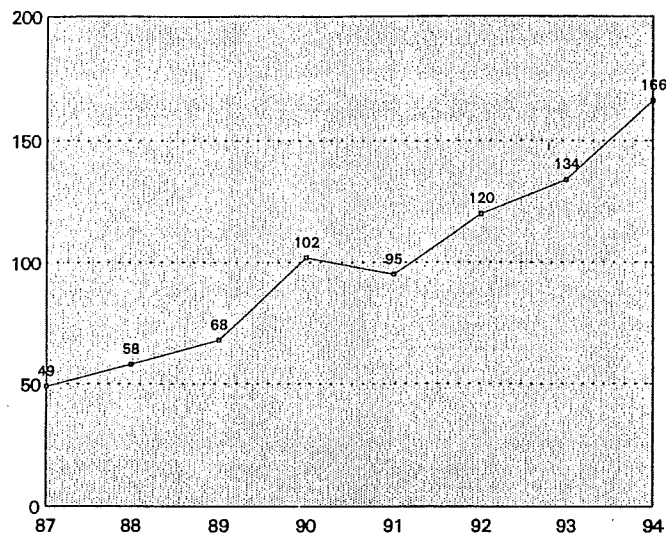
In successive years, as the Legislature passed laws relating to various aspects of credit and collection activity, it assigned responsibility for enforcing those laws to the Bureau of Consumer Credit Protection. As a result, the Bureau became the named enforcement agent in Maine's Fair Debt Collection Practices Act, Maine's Fair Credit Reporting Act, the Fair Credit Billing Act and the Plain Language Loan Act, as well as statutes relating to Mortgage Companies, Loan Brokers, Rent-To-Own companies and Pawnbrokers.

#### **5. Employees' Responsibilities**

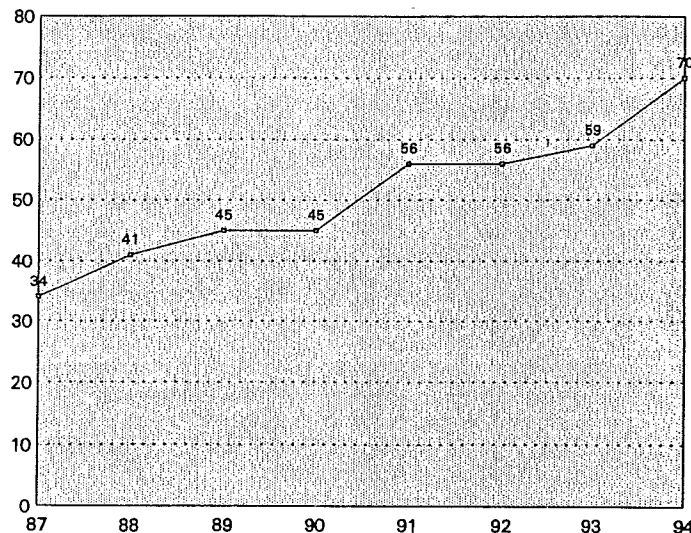
The Bureau administrator's title is "Superintendent of Consumer Credit Protection." The Superintendent's responsibilities include acting as hearing officer in administrative hearings (seven such hearings were held in

1993-94); preparing Bureau-sponsored legislation and appearing before legislative committees (primarily Banking & Insurance, and Business Legislation) to provide information on bills submitted by others; setting forth the Bureau's final determinations by way of formal Advisory Rulings on points of law (the current administrator has issued 12 such rulings); and providing general policy information to legislators, the Governor's administration and the media.

The Deputy Superintendent bears primary responsibility for processing license applications from Supervised Lenders (mortgage companies) and debt collectors. The numbers of applicants have risen dramatically in recent years, as demonstrated below:



Growth in Number of Licensed Supervised Lenders, 1987 - 1994

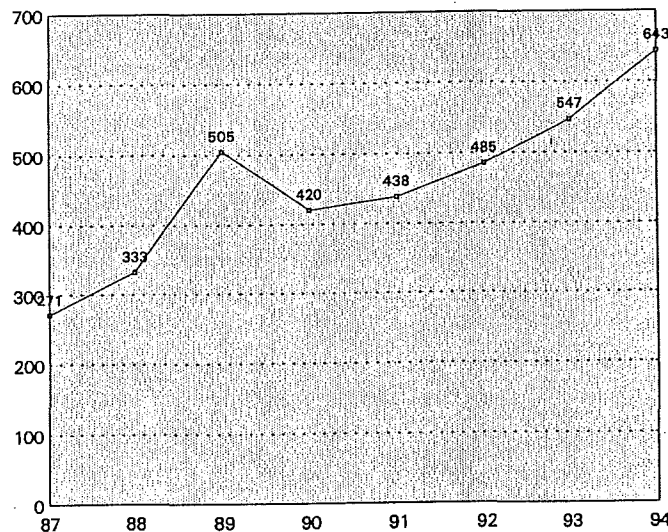


Growth in Number of Licensed Debt Collectors  
& Repossession Companies, 1987-1994

Review of Supervised Lender applications includes analysis of their financial health and stability, review of the consumer protection bond required of each main and branch office, and review of all lending documents related to products that will be offered to Maine consumers. For debt collectors, the review includes an evaluation of financial health, business and regulatory experience in other states, and all collection letters intended for use in this State.

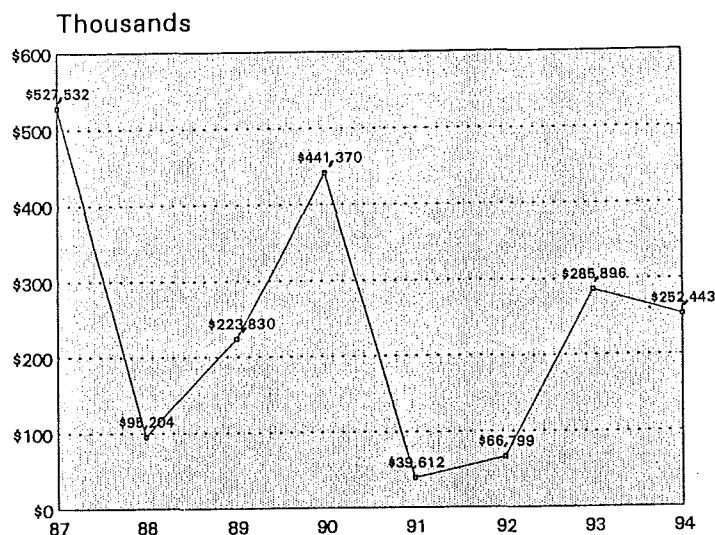
The Deputy Superintendent reviews examination reports of all regulated entities which involve significant violations, to determine whether those findings warrant an administrative hearing or the filing of a civil or criminal court complaint. In addition, the Deputy is responsible for certification of consumer loan and lease agreements under Maine's "Plain Language" law, 10 M.R.S.A. §1121 et seq.

One of the Bureau's Principal Examiners is responsible for the examination field staff, scheduling each of the examiners in order to maximize efficiency and minimize "down time" in the field. This employee responds daily to technical questions from creditors and lenders; receives, edits and finalizes Reports of Examination; and compiles exam statistics for use by the Bureau and for the information of affected businesses. This employee serves as the examiners' contact point in the office, advising the field staff on issues of law. In addition, the employee reviews and signs the 400 or more reports of examination delivered to Maine licensed and registered businesses each year, and, together with the Deputy Superintendent, determines whether and how to categorize violations found during examinations.



Growth in Number of Examinations Conducted, 1987-1994



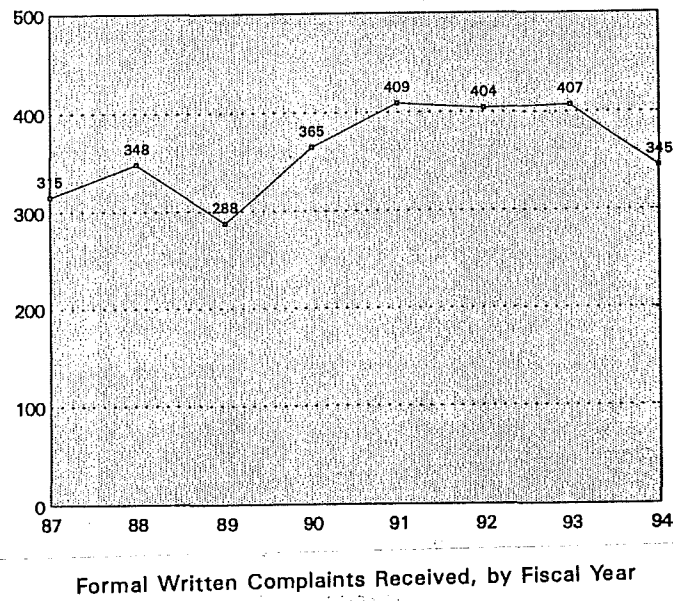
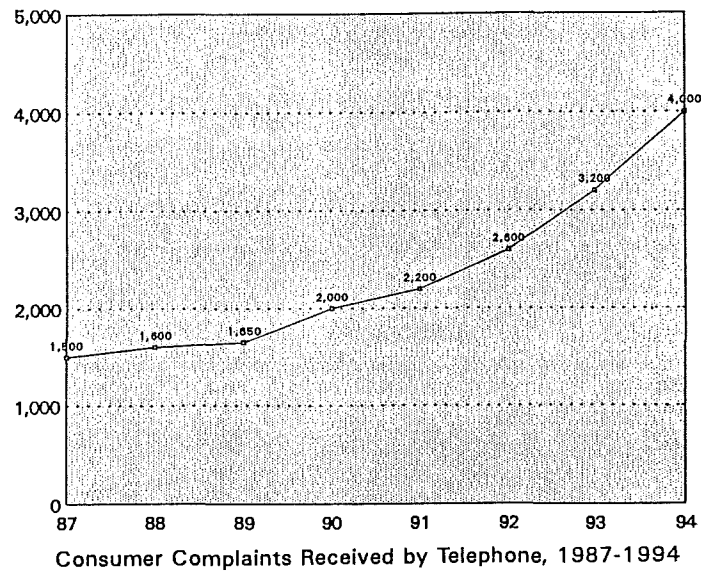


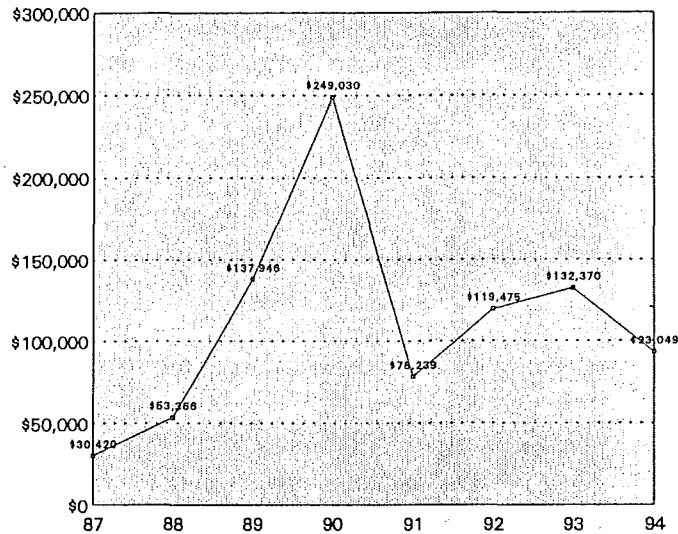
Monies Refunded to Consumers as a Result of Compliance Examinations, 1987-1994

The second Principal Examiner is responsible for more than 1,500 individual creditor filings. Each creditor serving consumers in Maine is responsible for compliance with laws relative to disclosure, advertising computation and collection. Those creditors register and submit volume fees to the Bureau each year. This employee is also responsible for development of budgetary policy recommendations within the agency, and has served as a primary administrative resource in the past two years with respect to budgetary review as the agency has had to lay off one employee and leave two additional positions unfilled for budgetary reasons. This employee has also served as a permanent member of the State's RETI (Rapid Employment and Training Initiative) team, counseling Maine citizens involved in mass lay-offs, especially in large-scale industrial downsizings.

The field exam staff consists of four Consumer Credit Examiners who are on the road approximately 90% of their time throughout Maine, New England and beyond, reviewing the practices of Maine-licensed and regulated entities. They must often follow Maine-issued loans onto the secondary market to ensure proper accounting for escrow accounts, interest payments and collection practices. Originally six in number, the field examination staff has been reduced by one-third to 4, partly by a layoff for budgetary reasons and partly because of the need to bring one examiner into the office to assist with the burgeoning numbers of written and telephoned consumer complaints.

Consumer complaints are handled by the Bureau's Outreach/Research Specialist, with the help of the in-house examiner. The sheer numbers of complaints have required application of specific procedures involving tracking written and telephoned complaints, providing acknowledgements to the consumers, and establishing strict schedules for creditor response.





Refunds to Consumers as a Result of Consumer Complaints, Fiscal Years 1987-1994

In addition, this employee performs the registration functions for two types of businesses: Credit Services Organizations (loan brokers) and Credit Reporting Agencies. The loan broker oversight function has consumed an inordinate amount of time in the past 24 months, because allegations of violations of law have resulted in the need to prepare for five testimonial hearings.

As of November, 1994 the secretarial staff consists of three individuals, two less than authorized by the Bureau's Legislative count. The Bureau has been unable to fill the vacancies with full-time employees because of budget constraints. However, Bureau secretaries have nonetheless been able to meet the workload through overtime, increased word-processing pre-drafting by administrative personnel, increased efficiencies through training, and use of temporary employees during high-volume registration and licensing seasons. In addition, the secretarial staff has actually increased its own responsibilities in several areas, accepting and learning new skills in computer data programming/retrieval and license application processing.

## **6. Legislative Mandate**

The specific charge to the Bureau, found in L.D. 591, PL 268 (1993) "An Act Related to Mortgage Companies," is as follows:

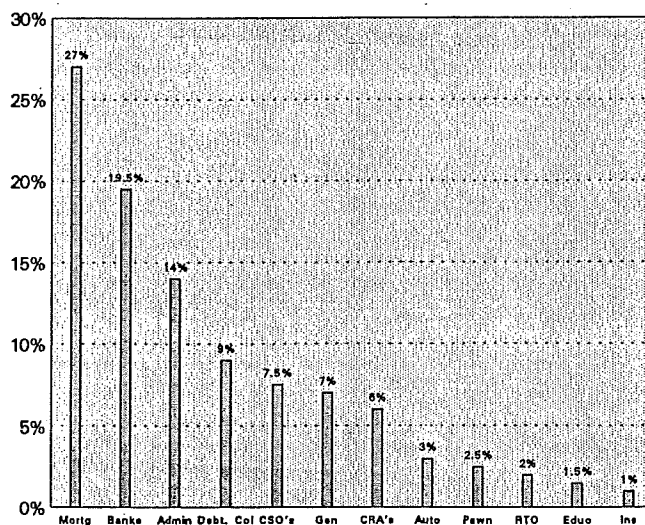
**Sec. 3. Report.** The Superintendent of the Bureau of Consumer Credit Protection shall report to the Joint Standing Committee on Banking and Insurance on or before January 1, 1995 on the following issues: 1) changing economic conditions; 2) the portion of staff time expended relative to various categories and sizes of business on complaint resolution, product review, consumer education and

enforcement activities; 3) the need for maintenance of adequate reserves without retention of excessive carryover balances; and 4) the bureau's administrative expenses in relation to the various categories and transaction volumes of lenders, lessors, sellers and assignees.

## 7. Results of Specific Studies

A. Mail Log. For several specific sample periods between April 8, 1993 and November 28, 1994, more than 350 items of incoming mail were analyzed in relation to the type of creditor involved. The results were as follows:

Mortgage Companies	27	%	CRAs (Credit Reporting	
Banks	19.5		Agencies	6 %
Administrative Issues	14		Auto Dealers	3
Debt Collectors	9		Pawnshops	2.5
CSOs (Credit Services			Rent-To-Own	2
Organizations)	7.5		Educational	1.5
General Creditors	7		Insurance Premium	
			Finance Companies	1



Mail Log Analysis by Subject Matter

- B. Telephone Log. Telephone call usage was analyzed to determine number of calls and length of call per type of consumer complaint. Below are the results from more than 700 minutes of phone calls:

Debt Collection:	22 % of total
Bank, including credit cards:	12
Repossessions:	12
Mortgage companies:	15
Credit Reporting Agencies:	8
Calls referred to the Attorney	
General (defective products, etc.):	6
Auto financing (dealer, bank, finance companies):	6
Scams:	3
Student loans:	3
Annual percentage rate question:	3
Loan brokers:	3
All Other (Cable TV, check cashing, warranty, financial planning, etc.):	7

- C. Consumer Complaints. Written consumer complaints have traditionally been recorded by type of complaint (e.g., Code violation, mortgage complaint). More recently, the Bureau has also maintained records of the type of business which is the subject of the complaint. The result of review of hundreds of such records is as follows:

1. By Creditor Type

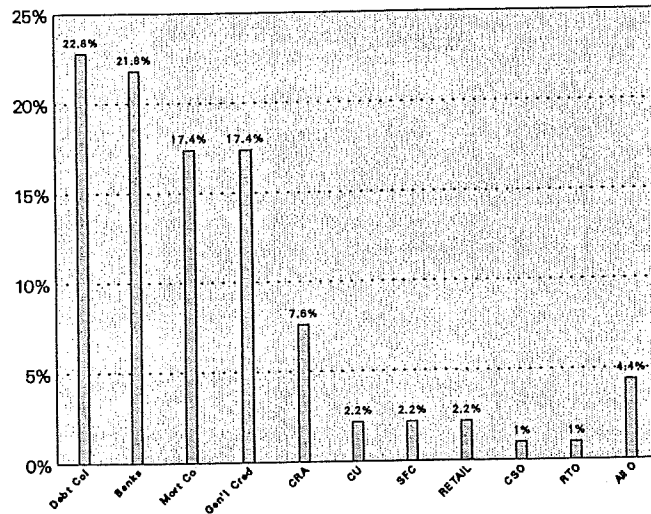
Debt Collectors:	22.8%
Banks:	21.8
Mortgage Companies:	17.4
General Creditors:	17.4
Credit Reporting Agencies:	7.6
Credit Unions:	2.2
Sales Finance Companies:	2.2
Retail Stores:	2.2
Credit Services Organizations:	1.0
Rent To Own	1.0
All Other:	4.4
	100. %

2. By Legal Violation Alleged

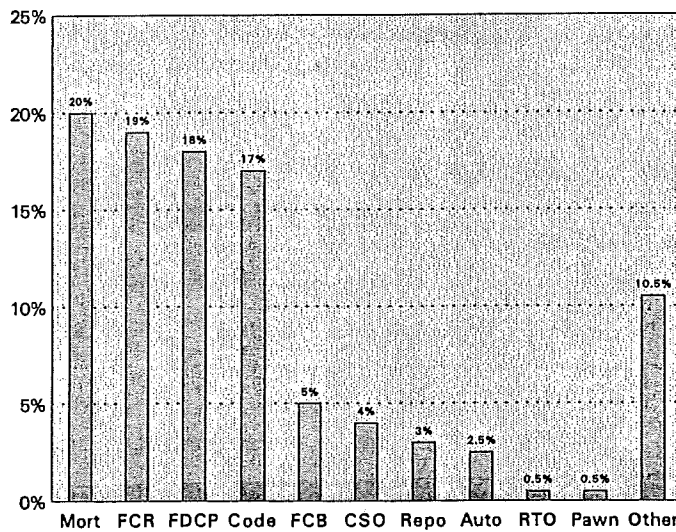
Mortgages(banks, credit unions & mortgage cos.):	20. %
Fair Credit Reporting Act (various creditors/lenders):	19.
Fair Debt Collection Practices Act:	18.
Consumer Credit Code (various creditors/lenders):	17.
Fair Credit Billing Act (usually credit cards):	5.

2. (continued:)

Credit Services Organization	
(loan broker) Act:	4. %
Repossession Law Violation:	3.
Auto Contracts:	2.5
Rent-To-Own Law:	0.5
Pawnshop Law:	0.5
All Other:	<u>10.5</u>
	100. %



Complaints by Creditor Type



Complaints by Subject Matter

**8. Income by Source**

Annual Bureau revenue from all sources now approximates \$900,000. That source is derived from a combination of volume fees, examination reimbursement, license fees and registration fees. A breakdown of those amounts by source follows:

a) Supervised Lenders (mortgage companies)			
License fees	\$ 20,000		
Examination fees	\$ 50,000		
Volume fees	<u>\$225,000</u>		
	\$295,000	(33%)	
b) Trust Companies			
Volume fees	\$150,000		
Exam reimbursement	<u>\$ 50,000</u>		
	\$200,000	(22%)	
c) Savings Banks			
Volume fees	\$ 70,000		
Exam reimbursement	<u>\$ 35,000</u>		
	\$105,000	(12%)	
d) Sales Finance Companies			
Volume fees	\$ 85,000		
Exam reimbursement	<u>\$ 7,000</u>		
	\$ 92,000	(10%)	
e) Merchant			
Volume fees	\$ 70,000		
Exam fees	<u>\$ 10,000</u>		
	\$ 80,000	(9%)	
f) Credit Unions			
Volume fees	\$ 20,000		
Exam reimbursement	<u>\$ 6,000</u>		
	\$ 26,000	(3%)	
g) Auto Dealers			
Volume fees	\$ 17,000		
Exam reimbursement	<u>\$ 10,000</u>		
	\$ 27,000	(3%)	
h) Collection agencies			
License fees	\$ 10,000		
Examination fees	<u>\$ 10,000</u>		
	\$ 20,000	(2%)	
i) Credit Services Organizations (loan brokers)			
Registration fees	\$ 4,000		
Examination fees	<u>\$ 4,000</u>		
	\$ 8,000	(<1%)	
j) Rent To Own			
Volume fees	\$ 3,000		
Examination fees	<u>\$ 2,500</u>		
	\$ 5,500	(<1%)	

k) Pawnbrokers

Volume fees	\$ 1,500	
Exam reimbursement	\$ 2,500	
	\$ 4,000	(<1%)

l) Savings & Loans

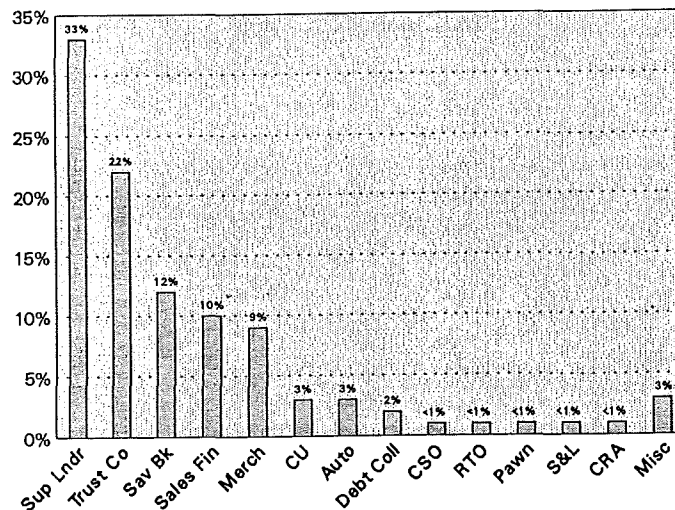
Volume fees	\$ 1,000	
Exam reimbursement	\$ 2,500	
	\$ 3,500	(<1%)

m) Credit Reporting Agency

Registration fees	\$ 1,500	
Exam reimbursement	\$ 1,500	
	\$ 3,000	(<1%)

n) Miscellaneous (Penalties;

Sales of Publications		
out of state; Plain		
language certification;		
etc.):	\$ 31,000	(3%)
	\$900,000	(100%)



Percentage of Bureau Revenue, by Business Type  
(Volume Fees, License Fees and Exam Fees Combined)

### 9. Reasons For Relative Shares of Revenue From Mortgage Company, Bank and Credit Union Activities

A review of the role of lenders in Maine provides a basis for understanding the reasons for the relative shares of the



Bureau's income generation from various entities:

A. Number of offices. 1993-1994 information includes the following totals for numbers of offices:

a) Trust Companies	258 offices and branches
b) Mortgage Companies	166 offices and branches
c) Savings Banks	158 offices and branches
d) State Credit Unions	<u>14</u> offices and branches

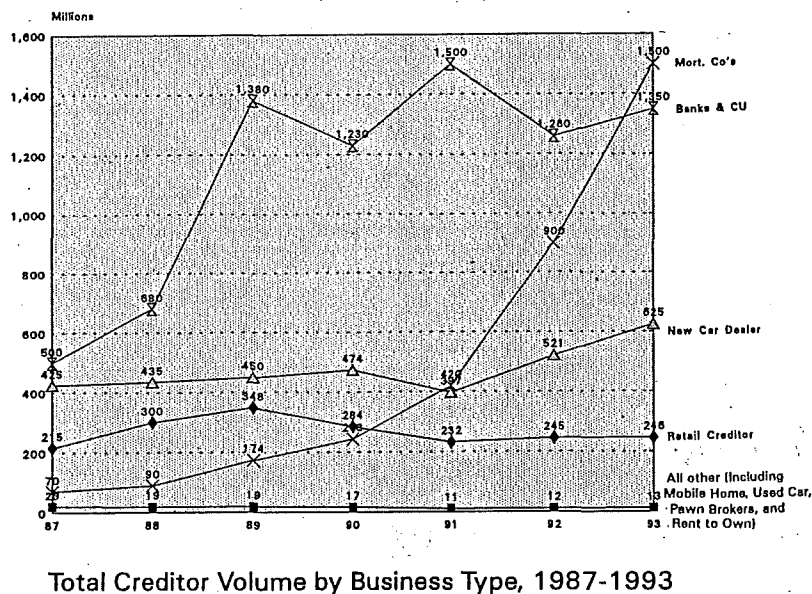
Total: 596

B. Volume

a) Trust Companies	\$ 870 Million
b) Savings Banks	\$ 390 Million
c) Mortgage Companies	\$1.504 Billion
d) State Credit Unions	<u>\$ 99 Million</u>

Total: \$2.863 Billion

The huge volume of business done by Maine's banks, mortgage companies and credit unions dwarfs that of other creditors, as illustrated by the chart below:



C. Complexity of products. Unlike new auto dealers who utilize standard credit sales forms, banks and mortgage companies offer a vast array of products for which the Bureau is responsible. They include:

a) Banks and Credit Unions: First lien fixed and adjustable rate mortgages (examined for Truth-in-Lending); second lien fixed and adjustable mortgages; small loans; unsecured open-end lines of credit; credit cards; home equity loans and construction loans.

b) Mortgage Companies: First lien fixed rate loans; first lien adjustable rate loans; discounted initial rate loans; "two-step" fixed and adjustable rate loans; construction loans; FHA, VA and MSHA-sanctioned loans; graduated payment loans; and "reverse" mortgages.

D. Significance to lenders and consumers. Unlike consumer problems and complaints relative to small purchases at retail creditors, issues involving banks and mortgage companies which come to the Bureau most often relate to loans secured by the largest assets owned by those consumers: their houses and their automobiles. The relative magnitude of these purchases increases the stakes for both the lender and the consumer. The result is that lenders seek determinations and opinions from top Bureau management, which increases the agency's expense. Additionally, consumers' urgency increases with the size of the loan at issue, likewise increasing Bureau expense in formulating a plan of assistance.

#### 10. Nature of Exam Violations by Creditor Type, and Consumer Refunds Following Examinations

Each year, the Bureau maintains its exemption from Federal Truth-in-Lending by providing the Board of Governors of the Federal Reserve information regarding its examination findings. The ten most common credit contract violations are as follows:

- Errors in Right of Rescission
- Failure to Disclose Annual Percentage Rate (APR)
- Failure to Disclose Finance Charge
- Incomplete Disclosure Statement
- No Disclosure Statement
- Understated APR
- Understated Finance Charge
- Other Incorrect Disclosures (Index Rate, etc.)
- Failure to Maintain Disclosure Records
- Disclosure Inconsistent with Note Terms

Among the more serious violations is that of "understated finance charge." The finance charge is the total cost of credit, expressed as a dollar amount. It is designed to put consumers on notice, for example, that their \$100,000 mortgage, repaid over 30 years at 10% APR, will cost them in excess of \$300,000 to repay. When a creditor understates a finance charge, the creditor misinforms the consumer of the true cost of credit. This happens in a variety of ways, predominantly by a creditor charging a consumer for extra cost items, without adding those charges to the disclosed finance charge.

A review of this single type of creditor violation reveals its ongoing occurrence:

**Understated Finance Charges  
Violation by Creditor Type**

<u>Creditor</u>	<u>Number of Violations</u>						
	<u>1987</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>
Trust Company	149	16	79	11	13	38	16
Savings Banks	60	19	22	32	29	26	343
Credit Unions	9	5	2	15	14	8	5
Supervised Lenders	45	129	37	9	27	36	29
Retailers	42	27	162	1	0	0	0

Many types of violations result in restitution to consumers. The basic rule of Truth-in-Lending is that a creditor cannot collect more of a finance charge than the creditor has told the consumer it would charge. If a creditor charges more in interest than it told the consumer in its disclosures at the time credit was extended, it must refund or credit the excess collected.

A review of refunds to consumers resulting from violations discovered during examinations, demonstrates that such errors are never completely eliminated, but also shows the strong incentive created by Truth-in-Lending for creditors to disclose the Annual Percentage Rate (APR) and Finance Charge correctly, and not try to hide additional charges by excluding them from these "cost of credit" figures:

Amount of Restitution

<u>Type of Creditor</u>	<u>1987</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>
Trust Companies	\$22,545.00	\$18,319.00	\$ 10,007.55	\$ 6,288.07	\$ 2,168.42
Savings Banks	900.00	1,732.00	1,160.41	2,595.38	35,134.87
Savings & Loans	0.00	0.00	7,394.45	0.00	0.00
Credit Unions	149.00	172.00	83.21	4,809.36	0.00
Supervised Lenders	19,785.00	8,605.00	375,584.37	17,484.00	2,740.54
Sales Finance	0.00	0.00	53.07	4.89	0.00
Retailers	15,984.00	5,056.00	420.20	8,430.20	5,239.16

<u>Type of Creditor</u>	<u>1992</u>	<u>1993</u>	<u>Total Restitution, 1987 - 1993</u>	
Trust Companies	\$121,144.41	\$13,206.66	Trust Companies:	\$193,679.11
Savings Banks	25,185.08	85,114.04	Savings Banks:	151,821.78
Savings & Loans	0.00	0.00	Savings & Loans:	7,394.45
Credit Unions	100.13	17,724.17	Credit Unions:	23,037.87
Supervised Lenders	19,930.28	95,441.04	Supervised Lenders:	539,570.23
Sales Finance	0.00	0.00	Sales Finance:	57.96
Retailers	61,718.15	0.00	Retailers:	96,847.71

**11. Assessment Gap: Unlicensed or Out-of-State Companies and Lenders**

One clear finding through the analysis of revenue sources to the Bureau compared to resources expended by the Bureau, is that there exists a certain level of subsidization of "the industry" by established firms. For example, license fees from collection agencies subsidize the Bureau's activities to protect consumers against out of state, unlicensed collectors harassing Maine consumers for debts allegedly incurred with distant creditors. In-state credit unions and banks partially fund the consumer complaint staff's handling of credit card complaints against federally-chartered institutions, which do not pay fees of any sort to the Bureau.

Sometimes, such enforcement actions against unlicensed entities can be expensive. If an out-of-state violator (collection agency, lender, credit clinic, etc.) does not initially respond to the Bureau's written request to reimburse a Maine consumer, the Bureau staff must use other resources at its disposal: regulatory and licensing contacts in other states; federal agencies (e.g., FTC; OTS; Board of Governors of the Federal Reserve and Comptroller of the Currency); and even national industry trade groups which have expressed a previous willingness to police their own association members.

The current legislative philosophy behind this partial subsidization includes the following:

1. In-state institutions benefit if their industry is kept "clean" and free of out of state operatives who do not respect Maine laws. Nearly every week, the Bureau exacts written assurances from out of state (and in-state) lenders, creditors, finance companies, credit clinics, repossession companies and other businesses that they will no longer attempt to operate in Maine without first obtaining necessary licensing or registration, and complying with Maine law. Through the Bureau's exclusion of non-compliant companies, various regulated entities benefit from the knowledge that they are competing on as level a playing field as possible.

2. Properly licensed and regulated companies benefit because they can operate with knowledge that those with whom they do business are likewise regulated, reducing exposure to private liability. The Bureau, through its various legislatively-assigned areas of responsibility, regulates nearly all stages of a credit transaction. This includes advertising; loan brokers; the credit reporting process; crediting of payments; rate change adjustments; early and initial disclosures; assessment of 3rd-party fees; accuracy of the charging of interest; procedures following default; repossession and collection. A mortgage company lending officer knows that the credit report process will be handled smoothly because of the Bureau's compliance examinations of all credit reporting agencies operating in Maine. A banker can hire a repossession company to retrieve an automobile from a defaulting consumer, with the knowledge that the reposses-

sion company, licensed and bonded by the Bureau, will not expose the lender to unnecessary liability through conduct resulting from ignorance of Maine's laws. Maine lenders selling mortgages on the secondary market may find that their time is not taken up handling servicing disputes from the sold loans, because of the Bureau's requirements that the new servicers print toll-free "800" numbers on all payment coupons.

## 12. Narrowing The Assessment Gap

Few viable funding alternatives exist if the Bureau is to remain a resource for Maine consumers. As discussed in this report, regulated industries pay approximately their fair share of reimbursable and overhead expenses. There are several exceptions to this rule. While collection agencies fully reimburse the Bureau for examination costs, and while license fees generally cover the cost of processing original and renewal applications, such agencies are not assessed a charge akin to the "volume fees" paid by creditors and lenders to cover the overhead costs of complaint investigation, advisory rulings and form approval. Likewise, the \$100 annual registration fee paid by credit reporting agencies does not cover the actual costs of responding to consumer questions and complaints.

Alternatives include:

A) Additional assessments against those companies. This may not be a realistic option, since Maine, through its examination functions and registration/license requirements, already has stricter regulation of collection agencies and credit reporting agencies than almost any other state. In addition, any such increases would merely be passed on to their customers, which are the Maine-based credit granters and lenders.

B) Assessment of per-complaint "investigation" fees. Already authorized by Maine law, these fees could and probably should be assessed more often by the Bureau, at least in cases of clear liability. However, many or most consumer complaints result from situations in which partial "fault" lies with both parties, or the problems result from a lack of communication between consumers and creditors. The Bureau encourages resolutions which favor the consumer, even in cases in which the regulated company is not willing to admit (and often vigorously denies) liability or wrongdoing. Attempted assessment of investigative fees in these cases could result in fewer informal, favorable outcomes for consumers.

In cases which result in administrative hearings, however, the Bureau staff in recent months has become more vigilant in accounting for its investigative expenditures, so that it may be in a position to request an order from the hearing officer for reimbursement, if the officer's decision favors the Bureau staff.

C) General fund appropriation. With a sizable shortfall already facing the general fund, this alternative is not likely to meet with popular support from the Legislature.

D) Refusal to respond to consumers' requests for assistance in cases involving unlicensed or out-of-state entities. Many federal "consumer assistance" agencies, and many agencies in other states, simply refuse to respond to individual consumer complaints in areas outside their specific regulatory authority. The Federal Trade Commission responds to consumer complaints with a form letter indicating that it does not intervene in such disputes, but that it will keep the consumer's letter on file in case a large-scale enforcement action is initiated at some future time.

The Bureau's experience is that this approach is not satisfactory to Maine consumers, nor to Legislators whose constituents often experience problems with out-of-state credit-related industries. Historically, the Legislature has supported the concept of maintaining the Bureau's ability to assist Maine consumers with credit problems, even if those problems result from the actions of distant assignees of Maine-made loans, or out-of-state credit card issuers or debt collectors.

### **13. Nature of New Lending Products, and Potential Delay In Regulatory Costs**

Although the Bureau receives volume fees on credit products based on the calendar year in which the credit is issued, the costs of regulation may not occur until years later. This is especially true when "boom" years of low interest rates are followed by recessionary and high-rate periods. A spurt in automobile sales in 1993 may be followed by a spate of default and repossessions in 1995, if employment rates do not improve. In addition, the interest costs on a sizeable portion of current real estate-secured products are based on the fluctuation of an index related to the prime rate. Rises in the index may add hundreds of dollars to monthly payments of consumers who took out first or second mortgages, or open-end home equity loans, when rates were low. With removal of interest rate caps on credit cards in 1994, variable rate credit cards will soon be prevalent in in-state and out-of-state banks. Increased interest costs based on those variable rates apply to existing balances, not just new purchases. In all these cases, lean economic times and increased interest requirements lead to more defaults, more collection activity and more requests for assistance from Maine consumers.

### **14. Complexity of Regulatory Issues Relative to The Differentiation in Assessment Totals**

The Bureau conducted a review of the issues routinely handled by the secretarial staff and the complaint staff,

compared to the issues which, by the nature of their complexity and the dollar volumes of the products in question, were referred to the Deputy Superintendent and Superintendent for resolution. The findings were not surprising: routine requests for information from general creditors were often handled by secretarial and consumer response staff, which results in lower overhead costs. Issues of interpretation and regulatory application vis-à-vis complex loan products from banks and mortgage companies were more commonly addressed to, or referred to, the most senior employees of the Bureau. Thus, when computing the resources necessary to regulate general creditors versus that necessary to oversee large-scale lenders of secured products (mortgage companies, banks and credit unions), an additional cost element must be factored into the calculations of actual cost.

#### **15. Procedures Undertaken To Meet Efficiency Goals**

In recognition of the changing nature of loan products being examined, and in response to improving results in the compliance examinations of several mid-size trust companies, the Bureau amended several exam-related procedures.

**A) Exam Scheduling.** Compliance exams for financial institutions have been conducted on an annual basis for the past decade. That period has been one of extreme change in bank products and procedures. Bureau examiners have seen certain institutions go through three complete changes of compliance computer software during that time. Mortgage products which were formerly customized for various borrowers and retained in bank portfolios, are now issued on uniform, multi-state documents which are packaged and sold on the secondary and tertiary market. Servicing is "stripped off" and contracted out by the investors to the lowest bidder. These changes have been the source of many systemic errors in bank compliance during this period, and bank compliance officers will confirm that examiners have performed tutorial functions on many occasions.

When the economy cooled off in 1993-94, however, certain institutions were able to apply more conscientious quality control programs to their consumer lending products, and compliance rates improved. For that reason, after consultation with the Superintendent in late 1993, the Principal Examiner in charge of scheduling established 18-month intervals for more than fifteen separate institutions. Those institutions, which were due for examination between the fall of 1994 and the fall of 1995, will not be contacted until late 1995 or early 1996. The increased time period came as a result of "no violation" or "minor violation" exam reports.

**B) Separation of Function.** In 1992, several meetings were held between exam supervisors from the Bureau of Consumer Credit Protection and the Bureau of Banking, designed to work toward the goal of eliminating any actual or apparent duplication of exam effort. One result of this consultation was Consumer Credit's deferral to the Bureau of Banking of the review of index rate change compliance by banks on first-lien adjustable rate mortgages (ARMs). Consumer Credit examiners, who are familiar

with index identities and fluctuations through their compliance work with those indices relative to first-lien ARMs made by mortgage companies, now share this information with Banking's examiners.

C) Concurrent Exams. Two years ago, the first concurrent examination was completed, with Consumer Credit and Banking examiners conducting a compliance review of a large, state-chartered bank with offices in Lewiston and Portland. Subsequently, the Bureaus' offer to schedule such a simultaneous exam was accepted by another bank. And in 1994, two more such exams have been conducted.

Although these events have been instructional for the examiners and have allowed bank compliance officers to be present on one occasion rather than on two separate schedules, the examinations also revealed considerably less overlap of review functions than had been previously been assumed. The single common area centered around first-lien adjustable rate mortgages: Consumer Credit reviewed the loans for Truth-in-Lending (early disclosures, initial disclosures, accuracy of closing statements and initial interest charge accuracy), while Banking reviewed the loans for compliance with that agency's Regulations #19 and #21. On the remaining loan products and procedures, the two teams found themselves diverging in terms of subject matter and eventually, location.

**PROTOCOL OF CONCURRENT EXAM - DIVERGENCE  
OF SUBJECT MATTER**

Consumer Credit Protection

- Residential mortgages - Truth-in Lending (Regulation Z)
- Credit card disclosure and limitation
- Home equity loans
- Adjustable rate second mortgages
- Credit denials, fair credit reporting
- Repossession and collection accounts
- Installment loans
- Dealer paper - assigned auto contracts
- Attorney selection law (2nd mortgages and home equities)

Banking

- First lien adjustable rate mortgages - disclosure and rate adjustments
- Advertising and charges - Savings and deposit accounts
- Funds availability
- Insider loans
- Attorney selection law (1st liens only)
- Emergency preparedness
- Demand notes

In the initial instance, Banking's staff was soon required to return to the institution's main office in Portland to interview bank personnel, while Consumer Credit's examiners remained at the Lewiston branch to review the actual loan products maintained.



Although the offer to schedule such concurrent exams has been made informally through the Bureau's newsletter, Creditor Update, the Bureau staff feels that the availability of such exams when practicable may become better known if formalized through the legislative process. For that reason, draft legislation submitted for the consideration of the incoming administration would give Maine-charted institutions the right to request such concurrent exams.

D) Modification of Exam Procedures. In recognition of the changing nature of financial institutions' record-keeping and loan processing, the Bureau in 1994 moved to direct its exam resources more to the computerized systems, with the result that a smaller sample of actual loans will need to be reviewed and the exam time will be utilized more efficiently. Examiners using their own portable computers, and accessing the bank's computers (through the cooperation of compliance officers) will utilize smaller samples, but track those samples through the origination, issuance, servicing and payoff functions. This is a step into the future, which may allow off-site examinations through remote access to the "platform automation" loan tracking systems utilized by banks and servicers. It is an acknowledgment that many modern bank errors tend to be in the computer system and software, as opposed to the clerical errors which marked the loan exam findings when products were handled individually and uniquely for each borrower.

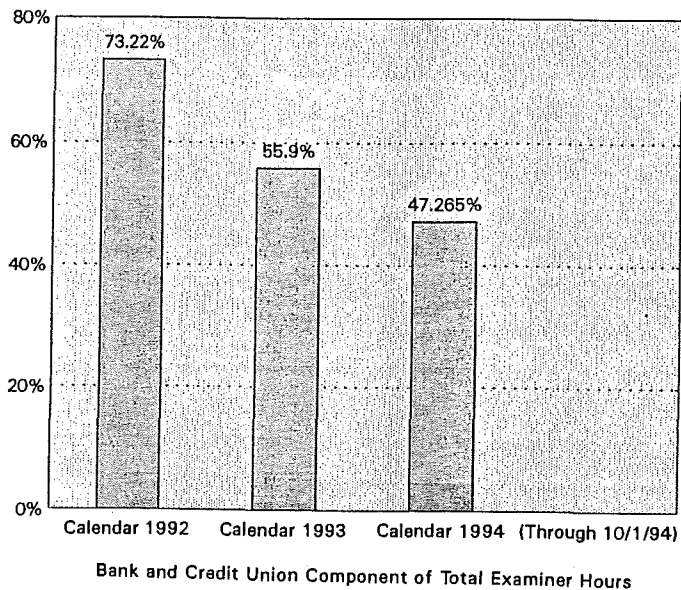
#### 16. Changing Composition of Exam Component; Examiner Hours Per Creditor Base

During the past 5 years, in response to consumer complaints and legislative requests for industry accountability, the Bureau has been assigned oversight duties in several credit-related areas. They include:

- registration and examination of credit reporting agencies;
- registration, examination, advertising, disclosure and collection requirements for rent-to-own companies;
- registration, bonding, examination, disclosure and contractual requirements for credit services organizations (loan brokers); and
- Truth-in-Lending examination of pawnbrokers.

During this time, the agency has shifted a portion of its overhead burden from supervised lenders (mortgage companies) and banks, to the newly regulated industries. An analysis of the time spent by Bureau staff on the examinations of various types of companies during the past three years, reveals that the agency has been successful in shifting its exam efforts toward the non-

bank component. The results of this analysis can be summarized by the chart below:



The data also demonstrates that the Bureau has effected this shift by scheduling an increasing percentage of examinations of a) retail automobile dealers; b) merchants who sell on credit; c) rent-to-own companies; d) credit services organizations; e) debt collectors; f) credit reporting agencies and g) pawnbrokers.

#### Percentage of Examiner Hours Per Creditor

<u>Business Type</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>
Retail Auto Dealers	6.56%	5.41%	11.92%
Sales Finance Companies	4.03	5.00	.17
Creditor Merchants	.95	----	7.45
Rent-To-Own	----	1.65	2.08
Credit Services Organizations	----	1.58	.79
Debt Collectors	1.27	5.28	1.19
Credit Reporting Agencies	.45	----	2.20
Pawnbrokers	----	----	3.96
Leasing Companies	----	.56	.36
Supervised Lenders	13.52	24.34	22.57
Investigations	----	.28	.05
<b>Total, Non-Banks/Companies</b>	<b>26.78</b>	<b>44.10</b>	<b>52.74</b>
Credit Unions	3.97	3.64	4.01
Savings and Loans	1.62	1.43	1.34
Savings Banks	30.40	21.30	16.19
Trust Companies	37.23	29.53	25.72
<b>Total, Banks/Credit Unions</b>	<b>73.22</b>	<b>55.90</b>	<b>47.26</b>
<b>Total All Types</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>

### 17. Additional Methods of Narrowing Assessment Gap

Additional methods of bridging the assessment gap include the following:

A) Cease subsidiary to non-profit lenders. Non-profit lenders (such as community action programs, or "CAPs") serving low-income residents are subsidized by other lenders under the current legislative scheme; see 9-A M.R.S.A. Article 2. Under law, their license fees are reduced to \$20.00. However, the products offered are often complex, including construction loans, waived interest products and due-on-sale clauses. The extra licensing and product review costs are borne by other regulated parties.

B) Charge fees for all product review. Currently, the Bureau encourages banks, credit unions, mortgage companies and other creditors (such as automobile dealers) to submit products for review prior to their use in Maine. Only in large-scale cases does the office routinely charge for this service.

C) Discontinue other non-revenue activities:

1) RETI Team. The Bureau has supplied a permanent member to the State's Rapid Employment Training Initiative (RETI) team, to help counsel workers who are losing their jobs in large industrial layoffs. Fifty-six such meetings have been held in the past 36 months, and the Bureau has covered all costs of salary and travel expenses for the agency's participation.

2) Seminars and training appearances. Members of the Bureau speak to various groups, including schools, industry or trade associations and consumer mediators. They fulfill several of the Bureau's legislative responsibilities (establishing programs for the education of consumers, and counseling companies as to their duties under the consumer laws; 9-A M.R.S.A. §6-104), but do not produce revenue for the agency.

3) Training. The Bureau's staff has benefitted from job-specific training (examination training; computer skills) and process-related training (TQM). Participation in quality-related activities alone has taken considerable time and resources during calendar year 1994. While these types of training will reduce costs in the long run, they are non-revenue-producing in the short term.

D) Amend law to allow charging for consumer booklets. Maine law currently requires the Bureau to provide educational booklets without charge to Maine consumers (9-A M.R.S.A. §6-203(4-A)). In the most recent fiscal year for which records were kept, 19,011 booklets were distributed in response to consumers requests. This becomes an overhead cost of the Bureau's operation. The Bureau favors continuation of the current policy, but feels that all costs should be identified in this report.

E) Encourage growth of small loan companies in Maine. In most other states, consumer credit regulatory functions are paid for through assessments on small loan companies and finance companies. Those companies have not found it profitable to establish offices in Maine, due to a law (9-A M.R.S.A. §2-308(3)) which caps the interest rate on high-interest, closed-end loans at 8% APR after 36 months. Other restrictions limit the number of profitable "ancillary products" (non-credit products) which can be sold along with a loan. Loosening these restrictions would allow small loan companies to return to this state. Those companies would pay fees to become licensed as supervised lenders, and would also pay volume fees based on the volume of money lent. (Whether or not to encourage the growth of such companies is a policy decision for the Legislature, and inclusion of this option should not be viewed as a Bureau endorsement. However, it is important to point out that consumer credit regulation in nearly every other state is funded in whole or in part by the non-bank small loan industry.)

F) Refuse to give advice on areas of non-responsibility. Creditors often request information on areas over which the Bureau does not have specific jurisdiction. The primary reason is that 1) legal advice is expensive if sought from private attorneys; and 2) the federal government, often the source of new, burdensome regulations, is often not reachable nor helpful in terms of specific, regulatory advice. A recent example of this example involves RESPA, the Real Estate Settlement Procedures Act. Bureau employees estimate they have received over 100 calls and inquiries from Maine lenders regarding this federal legislation during the 6-month period from May to November, 1994.

### 18. "Changing Economic Conditions"

A required component of this report is a discussion of the impact of "changing economic conditions" on the workload of the Bureau (PL Ch. 268 (1993)). The impact can be summarized by referencing several incidents in the recent past, and several predictions for the near future:

a) During periods of falling interest rates, purchases and refinancings increase. Consumer complaints to the Bureau focus on delays in closings, losses of lock-in fees and increased activity by non-lender loan brokers, or credit services organizations. License activity increases, as mortgage companies seek to take advantage of the activity by forming in Maine or by licensing an out-of-state office from which to solicit Maine consumers.

Falling rates mean increased credit reporting agency business, with the result that more credit report errors come to light. Consumer complaints to the Bureau increase during this time, and response time by companies may slow because of their increased workload.

b) During periods of rising interest rates, the availability of funds decreases and lenders tighten loan eligibility restrictions. Consumers who feel they were promised loans at certain rates, and who face delays which can put them beyond their rate lock period, become desperate and rely heavily on the Bureau for assistance. These cases are especially difficult for Bureau personnel, because lenders or brokers may lose their sources of funding or their secondary market purchasers, so that no easy remedies to the consumers' problems present themselves; i.e., whatever the cause of the delay, providing the consumer with a loan at the earlier, lower rate will require the direct outlay of funds by a lender, broker or third party.

Collection agency activity (and hence, the frequency of consumer complaints) rises during a tighter economy. Alternate sources of funds for consumers dry up, and more consumers experience delinquencies that will appear on credit reports, also generating an increasing number of calls to the Bureau.

Requests to the agency for new product review also increase during times of higher rates. For example, the past two years have brought the establishment and growth of "buy here, pay here" retail auto financing. Initiated by used auto dealers to combat lagging sales, these programs have meant that many dealers with no Truth-in-Lending compliance experience, have asked for Bureau assistance in drafting forms and developing quality control programs.

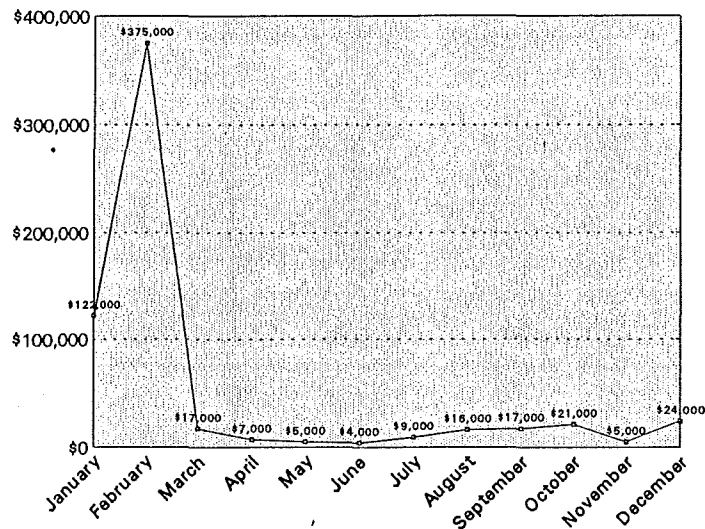
Finally, a tighter economy has led to the advent and growth of new types of industries. Rent-To-Own companies were almost non-existent five years ago, but their numbers swelled to more than 50 in 1993. Likewise, the pawnbroker business has grown to more than \$1.5 million in volume, as reported in Calendar Year 1993.

c) With respect to the topic of "changing economic conditions," an overriding principle to keep in mind is that the "volume fee" funding structure for the Bureau was designed to recognize that creditors' ability to pay increases as their volume (and profits) increase, and decreases as their business declines. All regulated creditors (whether auto dealers, banks or retail merchants) pay fees based on their yearly volume of credit business. When business declines, the Bureau must reduce expenses, and lay off employees or leave vacancies unfilled while searching for ways to increase the efficiency of its operations.

#### **19. The Need For Maintenance of Adequate Reserves Without Retention of Excessive Carryover Balances**

The Bureau receives the majority of its funds through volume fees at the end of January of each year. This money must last

throughout the calendar year and beyond, to the end of January of the following year.



Bureau Income Flow Through Calendar Year

For that reason, at the end of the State's fiscal year (June 30), the agency must still have approximately seven (7) months' reserves in order to avoid insolvency. In its early history, the Bureau actually borrowed from the Governor's Contingency Fund (forerunner of the "Rainy Day" fund) to meet payroll.

## **20. Conclusion**

The Bureau currently operates without any cost to the General Fund. Rather, the primary components of its funding structure are based upon volume fees (which increase or decrease based on the volume of business transacted) and exam reimbursement fees.

The Bureau routinely expends consumer assistance and other regulatory resources in areas for which it receives no direct reimbursement: helping Maine consumers deal with credit problems caused by lenders and creditors which are unlicensed or which are exempt from this State's jurisdiction. In addition, the law places various responsibilities and costs on the Bureau (consumer education; reduced-cost license fees for non-profit lenders) for which agency expenses must be absorbed.

Various steps may be taken to reapportion the costs among the regulated parties. Each such step will be met with support or resistance, depending on individualized impact and whether a certain industry segment's expenses are increased or decreased.

Any such steps, however, must be taken with complete knowledge of the tenuous and variable nature of the current revenue sources, and must recognize the measures already taken by the Bureau to amend its practices and assess costs to the industry based on efficiency of regulation and fairness of cost apportionment.