Federal Reserve Announces Consent Order Related to Bank’s Use of Discount Points

Article By:

Daniel C. Fanaselle

On November 28, 2017, the Federal Reserve Board announced a Consent Order with Peoples Bank (Peoples) in Lawrence, Kansas. The Order charges Peoples with violating Section 5 of the Federal Trade Commission Act (FTCA) by engaging in deceptive mortgage origination practices between January 2011 and March 2015. According to the Order, Peoples “often” gave prospective borrowers the option of paying discount points (an amount calculated as a percentage of the loan amount) at the time of closing, in order to obtain a lower interest rate. According to the Fed, this “regularly” led borrowers to pay thousands of dollars for discount points, but did not always result in a lower interest rate. Peoples denies the charges, but has agreed to pay $2.8 million to a settlement fund for the purpose of making restitution to the affected borrowers. Also, while not a part of the Order, Peoples has ceased taking new mortgage applications, and is in the process of winding down its mortgage lending operation.

Section 5 of the FTCA proscribes “unfair or deceptive acts or practices in or affecting commerce.” Here, the Federal Reserve found that Peoples’ misrepresentations were deceptive because they were likely to mislead borrowers to reasonably conclude that they obtained a lower interest rate through the payment of discount points, when in fact, many did not receive a reduced interest rate, or received a rate that was not reduced commensurate with the price they paid for the discount points. This was found to be material because it “relate[s] to the cost of the loan paid by the borrowers.

The Consent Order notes that Peoples’ loan disclosures “gave an accurate quantitative picture of the loans’ costs.” But according to the Fed, Peoples (which had no written policy regarding discount points) misrepresented and/or omitted the nature of the discount points, which led many reasonable consumers to incorrectly assume they were receiving a rate based on the discount points they paid, when they actually received no benefit (or not the full benefit) from their payment. This illustrates the need for mortgage lenders to ensure they are painting an accurate picture of their mortgage products at all stages of the origination process – including advertising, loan disclosures, and communications with prospective borrowers.

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