

LENDERS UPDATE™

A MONTHLY SERVICE TO THE MORTGAGE LENDING INDUSTRY

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Volume XIV

January 2007

Issue I

We wish all of you a happy and successful New Year.

The purpose of the Lenders Update is to provide a “heads-up” of new legislation and regulations affecting the mortgage lending industry. We try to provide brief summaries of new matters so our readers can judge whether the subject impacts their operations. We recommend that our readers review the entire new material in detail where relevant. For your convenience, the applicable statute, regulation or cases can be easily identified in the summary. Our Update includes changes in legislation available to Alt & Associates by January 15, 2007

FEDERAL ISSUES

NEW CHARM BOOKLET

Beginning in **October 1, 2007**, lenders will be required to use the newly published Federal Reserve Board CHARM Booklet. According to the FRB, the revisions are to ensure that consumers understand the risks for nontraditional ARMS. The new booklet includes discussions of the risks of these new products. Information is included concerning interest only loans, payment option ARMS and hybrid ARMS that include an initial fixed rate period with a longer adjustable rate. Additional new features include an expanded shopping worksheet, new examples, and information about “low doc” or “stated income” loans. A copy of the booklet can be obtained on the Federal Reserve Board website at www.federalreserve.gov

FANNIE AND FREDDIE FOLLOW NONTRADITIONAL MORTGAGE PRODUCT GUIDELINES.

As we know, in October of last year, the Federal Joint Agencies (OCC, FRB, FDIC, OTS and NCUA) issued inter-agency guidance on nontraditional mortgage product risks. The guidance discusses how institutions can offer nontraditional mortgage products in a safe and sound manner and in a way that clearly discloses the benefits and risks to the borrower. This was followed by a Conference of State Bank Supervisors, in conjunction with the American Association of Residential Mortgage Regulators, who issued guidance a month later that mirrors that of the joint agencies.

Then, in December 2006, Fannie Mae and Freddie Mac have taken immediate action to require steps be taken consistent with the guidance provided by these two groups. While the guidelines are more specific, Fannie and Freddie generally require lenders:

- Develop and implement written policies and specify acceptable product attributes, portfolio limits, sales and securitization practices, and risk management expectations.
- Design and implement internal controls to ensure that guaranteed mortgage purchases meet the underwriting and consumer protection standards of the guidance.
- Design and implement enhanced performance measures and management reporting that provide early warning for increased risk.
- Establish appropriate loan loss allowance levels that consider the credit quality of the portfolio and conditions that affect collectibility.
- Maintain capital commensurate with the risk characteristics of their nontraditional mortgage loan portfolios.

Once again, the joint agencies guidelines were published on October 4, 2006 in the Federal Register at Vol 71, No. 192.

FEDERAL TRADE COMMISSION EXTENDS FORBEARANCE POLICY OF TSR

On December 27, 2006, the Federal Trade Commission responded to a request for forbearance concerning the creation of a new safe harbor in the Telemarketing Sales Rule for pre-recorded seller and telemarketer calls to consumers with whom the seller has had an established business relationship. The FTC also proposed an amendment to the TSR that would make explicit the prohibition on pre-recorded calls that is not now implicit in the TSR's call abandonment position. The FTC previously had indicated it would not forebear enforcement of the prohibition effective January 2, 2007. However it has reversed that policy and has determined that the forbearance policy should remain in effect until the conclusion of the amendment procedure.

STATE ISSUES

MARYLAND

Montgomery County Lending Law.

As previously discussed, Maryland's Montgomery County passed legislation authorizing stiffer penalties against lenders and brokers who engage in predatory lending practices. Now, a Maryland judge has found that this law is unconstitutional. In an action brought by the American Financial Services Association, Judge Michael D. Mason issued a temporary injunction against the law. He found that the law has substantial territorial effect beyond just Montgomery County, and is unconstitutional. The case American Financial Services Association, et al., vs Montgomery County, Maryland, Civil Action # 269105 is filed in the Circuit Court of Montgomery County, Maryland.

MASSACHUSETTS

New Regulations Concerning Mortgage Lenders and Brokers

Effective **December 1, 2006**, Massachusetts has adopted 10 Prohibited Acts and Practices to its regulations governing mortgage lenders and mortgage brokers. This regulation supplements the emergency regulation adopted by Massachusetts in September 2006. For those of you doing business in Massachusetts, both new regulations should be reviewed in detail. They can be

found at www.mass.gov under Division of Banks, subsection on Predatory Mortgage Abuse as 209CMR42.00 and following sections. Specifically, the new Prohibited Acts and Practices can be found at 209CMR42.12A.

MICHIGAN

Adopts Best Practices for Nontraditional Mortgage Products

As indicated above, the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators adopted guidance resulting from the Federal Joint Agencies guidance on nontraditional mortgage products. As envisioned by these two groups, the new guidance would apply to state licensed mortgage brokers and companies. Now, the Office of Financial and Insurance Services in Michigan has issued a set of regulatory “best practices” governing the marketing of nontraditional mortgages by its licensed entities. Michigan’s regulatory guidance can be found on the OFIS website at www.michigan.gov/ofis under the menu item “What’s New”.

NEW YORK

Law on Loan Originators

On **December 6, 2006**, the New York Governor signed a law amending the Banking Act by adding Article 12-E, which regulates and requires the registration of loan originators. 12-E requires all persons who, while employed or while acting as independent contractors, act as loan originators for a Mortgage Broker or Banker, to register with the New York Banking Department by **January 1, 2008**.

This means that all persons who solicit, negotiate, explain or finalize the terms of a mortgage loan must be registered as loan originators. However, New York has clarified that solicitation does not include persons who simply take customer information and/or make referrals of customers to a Broker or Banker. N.Y. Banking Law § 599-B(2).

In addition to registering, the loan originator must also complete educational courses. Loan originators must complete 18 hours of educational courses within a year after registration has been approved. Thereafter, the loan originator must fulfill continuing education courses of 18 hours for every two years. This requirement lasts for the first 8 years the loan originator is registered with the Banking Department. After the first 8 years, the continuing education courses are reduced to 8 hours for every four years.

While registration is being approved, New York does allow the loan originator to engage in mortgage loan originating on a temporary basis. However, the Broker or Banker cannot permit a person to engage in mortgage loan originating unless the Broker or Banker has received notice from the Department that it has received an application and a copy of fingerprints for registration of that person.

RHODE ISLAND

New Predatory Lending Regulations

Rhode Island has published emergency regulations implementing and amplifying on the Rhode Island Home Protection Act which went into effect **December 31, 2006**. The regulations provide additional requirements as well as clarifications of the Act and will remain in effect until **April 30, 2007**. The temporary regulations discuss record keeping requirements, including records that must be kept to support and substantiate Tangible Net Benefit Analysis or High Cost Loan Analysis. They also detail provisions for additional disclosures in keeping with the Acts requirements. They further discuss counseling requirements and disclosures. The Act is effective as of **December 31, 2006**; however Rhode Island has announced that it will not take enforcement actions until **February 2007**. The new regulations can be found at www.dbr.ri.us under the “News” menu item identified as Bulletin, “Banking Regulation 3”. Again, please note that these regulations require a number of disclosures to be used for High Cost Home Loans in this state.

WASHINGTON

New Mortgage Broker Regulations

After a public hearing in October 2006, Washington State adopted new rules implementing its revised Washington State Mortgage Broker Practices Act. These became effective **January 1, 2007**. We have summarized these rules for your information, however the rules can be found at WAC208660 which can be located on the Washington State Department of Financial Institution’s website, www.dfi.wa.gov

General Licensing: Mortgage brokers and loan originators must obtain a valid Washington license, or be exempt, in order to originate residential mortgage loans. There is no “one time loan” exception.

The mortgage broker and loan originator license expires annually.

At any given time, the mortgage broker must appoint only one individual to be the designated broker. If the designated broker leaves, the licensee may continue to operate, however, the licensee must notify the department within 5 days of the loss of, or change of, the designated broker. The licensee must then replace the designated broker within 30 days.

Exemptions:

- Consumer Loan Act (“CLA”): If you are licensed under the Consumer Loan Act, any loans covered by that act are exempt from the Mortgage Broker Practices Act.
- Fannie Mae/Freddie Mac: Although a license is not required, entities subject to audit by Fannie Mae or Freddie Mac are subject to RCW 19.146.0201 through 19.146.080 and those rules associated with those sections of the act. Those sections include prohibited practices, certain required disclosures, the requirement of a writing for agreements, trust fund requirements, books and records requirements, limitations on fees or compensation and the requirement to provide the consumer with certain information for which the consumer has paid. You are also subject to investigation and enforcement authority of the director. Your loan originator employees (not 1099 contractors) are also not required to have a license, but again, they are subject to the above sections and rules.

- Independent Contractors: Independent contractors of licensed Mortgage Brokers are **not** exempt from licensing. After January 1, 2007, independent contractors, working as loan originators for an exempted mortgage broker, must obtain a loan originator license.

Mortgage Brokers: Fees: A mortgage broker may charge a fee, and may bring a suit for collection of the fee, not to exceed three hundred dollars for (1) services rendered (2) for the preparation of documents, OR (3) for the transfer of documents in the borrower's file which were prepared for, or paid for, by the borrower if;

- the mortgage broker has obtained a written commitment from a lender on the same terms and conditions agreed upon by the borrower and the mortgage broker, and
- the borrower fails to close on a loan through no fault of the mortgage broker, and
- the fee is not otherwise prohibited by the Truth in Lending Act.

Mortgage Brokers must file a mortgage broker annual report which is due by May 1st of each year beginning in 2007.

Designated Brokers: Designated brokers must pass the designated broker test and have a minimum of 2 years experience lending or originating residential mortgage loans. The designated broker does not have to be employed exclusively with one licensee. Each designated broker must complete 3 courses of no less than 3 hours for their continuing education requirement.

Loan Originators: Loan originators must pass the licensing test, submit an application and attachments and pay the appropriate fees. Loan originators must also complete continuing education courses in the form of two courses of no less than three hours each, annually. A loan originator may not charge the borrower a fee, commission, or compensation of any kind in connection with the preparation, negotiation, and brokering of a residential mortgage loan.

Recordkeeping Requirements: The following books and records must be kept and be available to the department:

- Mortgage Transaction Documents;
- Advertisements;
- Trust accounting records;
- All other books, accounts, records, papers, documents, files and other information relating to the mortgage broker operation.

The books and records must be kept for a minimum of 25 months. Books and records may be kept electronically, provided the following are met:

- The equipment must be made available to the department for the purposes of an examination or investigation;
- The records must be stored exclusively in a non-rewritable and non-erasable format;
- The hardware or software needed to display the records must be maintained during the required retention period.

Departmental Powers: The new rule provides that a licensee's business will be examined at least once during the first 5 years of licensing. 30 days notice will be given to routine examinations

but not for examinations prompted by consumer complaints or when the Department has reason to believe that the broker has violated the Act.

The protocols for examination are detailed in the Department's Mortgage Broker Examination Manual. Currently a draft of the manual is up on the Department's website.

Our monthly Lenders Update is published via e-mail as a complimentary service to our subscribers and clients in the financial industry throughout California and the United States. Our Lenders Update Manual: A Guide to State Mortgage Lending Law is available through our website at

www.altandassociates.com

Only those persons who have requested this newsletter are on our mailing list. Should you have colleagues who wish to receive this complimentary service, please have them e-mail us at

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ALT & ASSOCIATES provides regulatory, compliance and licensing services, operational advice and transactional assistance, as well as litigation representation, to the financial services industry. Over the past two decades, members of the firm have represented Institutional Lenders and Mortgage Bankers and Brokers in all aspects of their operations. If you have any questions please contact:

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