LENDERS UPDATE™

A MONTHLY SERVICE TO THE MORTGAGE LENDING INDUSTRY

AN ALT & ASSOCIATES NEWSLETTER

Main Office:
2102 BUSINESS CENTER DRIVE
SUITE 130
IRVINE, CA 92612

Mailing Address:
P.O. BOX 4125
IDY, CA 92549-4125

DAVID JEROME ALT
Attorney at Law
David.j.alt@altandassociates.com

TELEPHONE 949.253.5755
FACSIMILE 949.253.5756
www.altandassociates.com

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The purpose of the Lenders Update is to provide a "heads-up" of new legislation and regulations affecting the mortgage lending industry. We provide summaries of new matters so our readers can judge whether the subject impacts their operations. We recommend that our readers review the entire new statute, regulation or other material in detail where it is relevant to them. For convenience, the applicable matter can be easily identified in the summary, and, where possible, a link is provided.

The Update includes information available to Alt & Associates as of July 29, 2010.

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CURRENT MORTGAGE RELATED PROVISIONS CONTAINED IN THE RESTORING AMERICAN FINANCIAL STABILITY ACT 2010

Over the past 6 months we have been watching the interplay between the House and the Senate as they have considered HR 4173, the Restoring American Financial Stability Act ("RAFS") and other versions of the same legislation. As you may know, last week the Joint Conference Committee of the Senate and the House appeared to finalize RAFS. The bill was to be voted on by both houses of Congress. However, new opposition in the Senate has prevented reaching the magic 60 vote Senate requirement to stop debate and bring the matter to vote. These objections, which as of this date appear to be resolved, were

Republican objections to the 19 billion dollar banking fee. It now looks as though the final passage will be delayed for a week or ten days.

Nonetheless, we hear from our clients and friends great concern as to the Act's content and the dramatic effect that it may have on the mortgage industry. As a result, we thought we would briefly summarize the Act's mortgage lending related sections as they stood at the end of last week. When the bill passes, we will provide a new and final summary

PROHIBITED PAYMENTS OF MORTGAGE ORIGINATORS

- **Any consumer credit transactions secured by real property may not allow the originator to receive from any person, directly or indirectly, compensation that varies based on the terms of the loan (other than the amount of the principal).**
- **A loan originator may not arrange for a consumer to finance through the rate, any origination fee or cost except bone fide third party settlement charges not retained by the creditor or loan originator. Exceptions to this rule are that a consumer may finance, through the rate, an origination fee if:**
    - **the loan originator does not receive any other compensation, directly or indirectly,**
    - **no third party person pays any compensation to the loan originator, directly or indirectly, in connection with the transaction, if that person has reason to know that a consumer paid compensation to the loan originator, or**
    - **the consumer does not make an upfront payment of discount points, origination fees, or points or fees, however denominated.**
- **These rules do not apply,**
    - **to limit the compensation received by a creditor upon the sale of a consummated loan to a subsequent purchaser,**
    - **to restrict the consumer's ability to finance, at the option of consumer, through principal or rate, any origination fees or costs, so long as such fees or costs are not based on the terms of the loan other than the amount of the principal, or**

- **to prohibit incentive payments to the loan originator based on the number of loans originated within a specified period of time.**

- **Loan originator means a person who, for gain,**
  - **arranges for an extension, renewal or continuation of credit,**
  - **takes an application for credit or assists the consumer in applying for such credit or offers, or**
  - **negotiates terms of such credit.**

MINIMUM STANDARDS FOR RESIDENTIAL MORTGAGE LOANS

- **No creditor may make a loan secured by real property or a dwelling unless, based upon verified and documented information by which the creditor determined, at the time the loan is consummated, that the consumer has the ability to repay the loan according to its terms as well as pay all applicable taxes, insurance and assessments. The new Act sets out the minimum basis for such determination and the items to be considered including detailed provisions as to income verification.**
- **Any creditor is entitled to the presumption of the ability to repay if it has complied with these provisions and has determined that the consumer has the ability to repay, using the maximum rate permitted under the loan during the first 5 years, a payment schedule that fully amortizes the loan and takes into account current obligations, and all applicable taxes, insurance and assessments.**
- **The presumption would not apply where,**
  - **the regular periodic payments result in an increase of the principal balance or allow the consumer to defer repayment of principal,**
  - **the terms result in a balloon payment (A balloon payment is a scheduled payment more than twice as large as the average of the earlier scheduled payments.), or**
  - **the total points and fees payable in connection with the loan exceed 3 % of the total loan amount. Points and fees are defined in the Truth and Lending Act except to exclude fees for mortgage guarantee insurance, provided by an**

agency of the Federal government or an agency of a state, which are greater than 1 % of the loan amount.

Bridge loans and reverse mortgages are excepted from these provisions.

PROHIBITION ON CERTAIN PREPAYMENT PENALTIES

For purposes of prepayment penalty restrictions or prohibitions, the Act sets out a definition of a qualified mortgage, which means any residential mortgage loan that:

- **Does not have an adjustable rate**
- **Does not allow a consumer to defer a repayment of principal or interest**
- **Does not provide for a repayment schedule that results in negative amortization**
- **Does not provide for a balloon payment as defined above**
- **Which has an annual percentage rate which does not exceed the average "prime offer rate" for a comparable transaction as of the date at which the interest rate is set by 1.5 or more percentage points, in the case of a first lien residential loan, where the original principal obligation is equal to or less than the amount of the maximum limitation for a mortgage as set forth in the Federal Home Loan Mortgage Corporation Act**

Where a loan is not a qualified mortgage, it may not contain prepayment penalties.

If it is a qualified loan, then it may contain a prepayment penalty which cannot exceed the following guidelines:

- **During the first 1 year period, beginning on the date on which the loan is consummated, an amount equal to 3 % of the outstanding balance**
- **During the second 1 year period an amount equal to 2 % of the outstanding balance of the loan**
- **During the 3rd year period, an amount equal to 1 % of the outstanding balance**
- **No prepayment penalty can be charged after the end of the 3 year period**
- **A creditor must not offer a consumer a residential mortgage loan product that <u>has</u> a prepayment penalty without offering the consumer a residential mortgage loan product that <u>does not</u> have a prepayment penalty.**

- **A "primary offer rate", for purposes of this provision means an annual percentage rate derived from average interest rates, points and other loan pricing terms currently offered to consumers by a representative sample of creditors. This will be published at least weekly, by the Board of Governors of the Federal Reserve System.**

We will have the summary of the final legislation when it is passed.

Our monthly Lenders Update is published via e-mail as a complimentary service to our friends and clients in the financial industry throughout California and the United States. 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

sherry.edwards@altandassociates.com

ALT & ASSOCIATES provides regulatory, compliance, 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:

David J. Alt, Esq.

David.j.alt@altandassociates.com

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www.altandassociates.com