

# LENDERS UPDATE™

A MONTHLY SERVICE TO THE MORTGAGE LENDING INDUSTRY

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## AN ALT & ASSOCIATES NEWSLETTER

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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 21, 2010.**

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## **FINAL MORTGAGE LENDING PROVISIONS** **CONTAINED IN THE** **DODD-FRANK WALL STREET REFORM AND** **CONSUMER PROTECTION ACT** **(H.R.4173)**

Over the past 6 months we have been watching the interplay between the House and the Senate as they have considered HR 4173, now known as the Dodd-Frank Wall Street Reform and Consumer Protection Act and other versions of the same legislation. At the end of June, the Joint Conference Committee of the Senate and the House appeared to finalize Dodd-Frank. The bill was to be voted on by both houses of Congress. However, new opposition in the Senate prevented reaching the magic 60 vote Senate requirement to

stop debate and bring the matter to vote. These objections were resolved. After approval by the House, on 7/15/10 Dodd-Frank passed the Senate and President Obama signed the legislation into law on July 21, 2010.

The legislation, in the form presented to us, is well over 2000 pages in length, covering a range of subjects. Even at that, particularly as it relates to mortgage lending, most of the content will be fleshed out by regulations. These regulations will be formulated and presented for comment over the next couple of years. We will know more detail as this process develops.

The following briefly summarizes some of the most important portions of Dodd-Frank as it relates to mortgage lending.

#### **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). This provision is intended to prevent “steering” to particular loan products or programs.
- Compensation may be paid based on the principal amount of the loan.
- A person other than the consumer is not prevented from paying a fee:
  - If originator does not receive compensation from consumer,
  - Other than bonafide third party charges, the consumer does not pay other fees such as discount fees, origination fees, etc.
- 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.
- For purposes of these provisions, the term 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,
  - negotiates terms of such credit.
- The term loan originator does not include, among others:
  - a person who performs only real estate brokerage,
  - a person who performs clerical or administrative functions,
  - a servicer,
  - a creditor, except in a table funded transaction.

#### **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 the creditor determines 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 credit history, current income, expected income that consumer is reasonably assured of receiving, current obligations, DTI ratio and employment status.
- Where a creditor knows or should know the consumer will make more than one loan secured by the same residence, the creditor must, in good faith, determine that the consumer has the reasonable ability to repay the multiple loans.

**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 increase principal or allow the debtor to defer principal,**
- **Does not include balloon payments (regulations may be adopted to allow balloon payment under special circumstances),**
- **Has a borrower who has the verified ability to repay,**
- **Does not exceed the DTI ratios to be determined by the new Consumer Financial Protection Bureau (CFPB),**
- **Has a loan term not to exceed 30 years, and**
- **Has points and fees not in excess of 3% (point and fees are determined pursuant to a definition set out in the new statute). The CPBD is to adopt rules to adjust this 3% limitation for smaller loans**

**When the loan is a qualified loan, a borrower is presumed to have the ability to repay, although this is a rebuttable prescription.**

**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, and**
- **During the 3<sup>rd</sup> 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 has a prepayment penalty without offering the consumer a residential mortgage loan product that does not have a prepayment penalty.

#### **HOEPA or High Cost Mortgages**

- **HOEPA's provisions are expanded to home purchase loans.**
- **HOEPA's triggers are adjusted to:**
  - **Greater than 6.5 percent above the threshold for 1<sup>st</sup> liens and 8.5 percent for subordinate lien loans or points and fees exceed 5 percent**
  - **These triggers can be adjusted within limits, by the Federal Reserve Board.**
  - **The definition of points and fees is greatly expanded to include among other items, all compensation paid by the consumer or creditor and prepayment penalties.**
  - **Other restrictions or prohibitions for high cost mortgages have been added, such as:**
    - **Balloon payments and prepayment penalties are prohibited.**
    - **Late fees are limited to 4% and may not pyramid.**
    - **Modification or deferral fees are prohibited.**
    - **Pre-loan counseling before making a high cost loan is required.**

#### **EFFECTIVE DATE**

To say that the Effective Date of the provisions of the new act is uncertain is an understatement. Generally, most provisions of Dodd-Frank, as they relate to mortgage lending, must be implemented by regulation before becoming effective. These new regulations will probably not be effective for a lengthy period of time. Up to 3 years is possible.

**No need to panic yet.**

<p><b>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</b></p>
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**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:

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