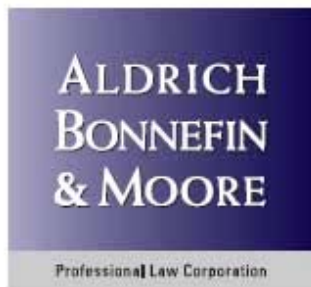


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FRB Hard at Work Amending Regulation Z and Proposing New Requirements

The Federal Reserve Board released several separate announcements August 16, 2010 amending several provisions of Regulation Z, primarily with respect to mortgage loans. In addition, the FRB has issued two new proposed rules dealing with escrow accounts for jumbo loans and also enhanced disclosures for mortgage loans. The following is a brief summary of the new rules. These rules will be covered in depth at future BCG Monthly Telephone Briefings. In the meantime, BCG members and other clients may contact Aldrich Bonnefin & Moore for specific advice.

Mortgage Transfer Disclosure Final Rule – Mandatory Compliance Date January 1, 2011

The FRB has adopted final rules to implement statutory amendments made to the Truth in Lending Act (TILA) requiring notification to consumers when the consumer's mortgage loan is sold, transferred or assigned. Recall that the FRB adopted an interim rule in November 2009 to implement the provisions of the Helping Families Save Their Homes Act of 2009 (the Act), which amended the TILA to establish this disclosure requirement. In general, any person or entity that acquires ownership of an existing consumer mortgage loan, whether closed-end or open-end consumer credit, that is secured by the consumer's principal dwelling must notify the consumer in writing no later than 30 days after the date on which the loan was sold, transferred or assigned. Note that although the provisions of Act were effective immediately upon enactment (May 20, 2009), and did not require the issuance of implementing regulations, the FRB nevertheless adopted an interim rule in November 2009 to provide guidance on how to interpret and comply with the statutory requirements. The FRB's recent action now makes final these provisions.

The notification requirements apply to "covered person," defined as any person, including natural persons and organizations such as corporations and partnerships, that becomes the owner of an existing mortgage loan by acquiring legal title to the debt obligation, whether through a purchase, assignment, or other transfer, and who acquires more than one mortgage loan in any 12-month period. To allow applicable lenders time to make any necessary operational changes, the final rule states that lender may continue to follow the November 2009 interim rule but only until the mandatory compliance date for the final rule, which is January 1, 2011.

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For a detailed discussion of the interim rule, refer to BCG Standard Procedures Manual #18, *Truth in Lending*, Part Three, Section XIX.

Tabular Format for Closed-end Mortgage Costs Interim Final Rule – Compliance Optional Until January 30, 2011

An interim final rule has been issued that implements certain additional requirements of the Mortgage Disclosure Improvement Act of 2008 (MDIA). The MDIA applies to all closed-end mortgage loans secured by a consumer's dwelling (and is not limited to adjustable rate mortgages (ARMs) or transactions secured by a principal dwelling). Portions of the MDIA have already been incorporated into Regulation Z, including the requirement that creditors provide early Regulation Z disclosures within three business days of receiving a consumer's written application but at least seven business days before consummation of the loan.

In addition to the early Regulation Z disclosure rules, the MDIA also requires creditors to disclose examples of rates and payments, including the maximum rate and payment. The Fed is adopting an interim final rule to implement these provisions. More specifically, the interim rule requires creditors that make consumer loans secured by real property or a dwelling to disclose certain summary information about interest rates and payment changes in a tabular format. The interest rate and payment summary tables replace the payment schedule that lenders are used to disclosing as part of the TILA disclosure, but only for mortgage transactions. Disclosures for non-mortgage, closed-end consumer credit will continue to include the current payment schedule. In addition to the summary table, the interim rule also requires creditors to include a statement that consumers are not guaranteed to be able to refinance their transactions in the future. The Fed has adopted model form and clauses for use in meeting the tabular format provisions of the interim final rule.

While the interim final rule will become effective once published in the *Federal Register*, compliance is optional until January 30, 2011. On that date, the provisions of the interim final rule will become mandatory for closed-end mortgage applications that are received on and after January 30, 2011.

Unfair, Abusive or Deceptive Loan Originator Compensation Practices Final Rule - Effective April 1, 2011

In an effort to protect consumers from unfair or abusive lending practices that can arise from certain loan originator compensation practices, the Fed has adopted a final rule that essentially places restrictions on how mortgage brokers and loan originators are compensated. The final rule becomes effective April 1, 2011.

The final rule stems from a proposed rule issued by the Fed in August 2009 (74 FR 43232). The proposed rule would have prohibited certain compensation payments to loan originators as well as steering consumers to loans not in their interest in an effort to receive greater compensation. Note that provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Reform Act") also amended TILA to impose compensation restrictions. In particular, the Reform Act creates new TILA Section 129B(c), which imposes restrictions on loan originator compensation and on steering by loan originators. While many of the provisions in TILA

Section 129B(c) are similar to the Board's proposed rules, the Reform Act also contains provisions not addressed by the proposal. As such, the Fed has determined to issue this final rule on loan originator compensation and steering, even though a subsequent rulemaking also will be necessary to implement new TILA Section 129B(c).

In general, the final rule:

- Applies to all persons who originate loans, including mortgage brokers and the companies that employ them, as well as mortgage loan officers employed by depository institutions and other lenders.
- Applies to closed-end loans secured by a consumer's dwelling or real property that includes a dwelling.
- Prohibits payments to the loan originator that are based on the loan's interest rate or other terms. Loan originators are permitted, however, to receive compensation that is based on a fixed percentage of the loan amount.
- Prohibits mortgage brokers or loan officers from receiving payments directly from a consumer while also receiving compensation from the creditor or another person.
- Prohibits "steering" a consumer to a lender offering less favorable terms in order to increase the mortgage broker's or loan officer's compensation. The Fed is adopting a safe harbor to facilitate compliance with the anti-steering rule. Under the safe harbor certain conditions must be met, including providing the consumer with loan offers for each type of transaction in which the consumer expresses an interest.

Proposed Rule Regarding Escrow Account Requirements for Jumbo Mortgages

A proposal has been issued that would implement provisions of the Reform Act (*i.e.*, the Dodd-Frank Wall Street Reform and Consumer Protection Act). Specifically Section 1461 of the Reform Act amended the TILA to provide a separate, higher threshold for determining whether an escrow account must be established for collecting property taxes and insurance on higher-priced mortgage loans. The Reform Act provisions, however, apply only to loans that exceed the maximum principal balance eligible for sale to Freddie Mac – that is "jumbo loans."

Recall that in July of 2008, the Fed adopted final amendments to Regulation Z that establish a new category of "higher-priced mortgages." Section 226.35 of Regulation Z (not to be confused with "high-cost" mortgage loans governed by Section 226.32) defines a higher-priced mortgage as a consumer-purpose closed-end loan secured by the consumer's principal dwelling having an annual percentage rate (APR) of 1.5 percentage points (first lien) or 3.5 percent percentage points (junior lien) or more above the "average prime offer rate" as published by the FRB. Among other things, lenders are prohibited from extending a higher-priced mortgage loan secured by a first lien unless an escrow account is established before consummation for payment of property taxes and premiums for mortgage-related insurance required by the creditor. Under the rule being proposed by the Fed, for "jumbo loans" the applicable threshold would be 2.5 or more percentage points greater than the average prime offer rate. The proposed rule would make

clear that this higher proposed threshold would apply solely for purposes of determining whether a jumbo loan is subject to the escrow requirements currently required under the regulation.

There will be a 30-day period for commenting on the proposal once it is published in the *Federal Register*.

Proposed Rule to Enhance Protections and Disclosures on Mortgage Transactions

Finally, the Fed has issued a proposal that would incorporate changes based on issues observed by the agency as a result of a comprehensive review of certain provisions of Regulation Z. The proposal is intended to improve various provisions of Regulation Z. Among other things, the proposed rule would:

- Simplify and improve rescission notices by: (i) revising the list of disclosures that if not properly made can trigger an extended right to rescind; and (ii) clarify creditors' obligations when the extended right to rescind is asserted in an effort to reduce uncertainty and litigation costs.
- Require new disclosures when the parties agree to modify the key terms of an existing mortgage loan.
- For closed-end mortgage loans, require lenders to refund fees if the consumer decides to withdraw the application within three days after they receive the required early Regulation Z disclosures.
- Require loan servicers to provide the information about the owner of the loan within a reasonable time after receiving a request from the consumer, which generally would be 10 business days.
- Conform advertising rules for home-equity lines of credit to rules adopted in 2008 for closed-end mortgage loans.
- Improve disclosures required to be provided in connection with reverse mortgages. For example, creditors would be required to provide a new, two-page disclosure which highlights in simple language the basic features and risks of reverse mortgages. In addition, creditors would be required to provide transaction-specific disclosures, in a tabular format, that reflect the actual terms of the reverse mortgage being offered. Also, at least three days before closing the loan, creditors would be required to provide final disclosures in the same format, to facilitate comparison with the earlier disclosures.
- Prohibit certain unfair practices in the sale of financial products with reverse mortgages.

There will be a 90-day period for commenting on the proposal once issued in the *Federal Register*.