

# The Federal Reserve Board's New Consumer Protection Rules for Mortgages

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Federal Reserve Board

# Goals

- Protect consumers from abusive, unfair, or deceptive acts or practices
- Preserve consumers' choice and their access to responsible credit

# Statutory (HOEPA) Authority

- Board shall prohibit acts or practices in connection with
  - Mortgage loans that are unfair or deceptive, or designed to evade HOEPA
  - Refinancings of mortgage loans that are associated with abusive lending practices or not in the interest of the borrower

# Overview

- Stricter regulation of underwriting practices and loan terms on higher-priced loans
- Protections for most mortgage loans in appraisals and servicing
- Advertising requirements and restrictions
- Earlier disclosure of loan terms

# Higher-Priced Loans

- Assessment of repayment ability for every loan
- Verification of income or assets relied on
- Escrows for taxes and insurance
- Prepayment penalty prohibitions and restrictions

# Higher-Priced Loans

## *Definition*

- 150 bps over average prime offer rate
  - 350 bps for subordinate lien loans
  - Change from proposal which relied on Treasuries
- Expected to cover all subprime loans and some alt-A
- A few exceptions, e.g., HELOCs

# Higher-Priced Loans

## *Repayment ability*

- Prohibits making a loan based on collateral without regard to the borrower's ability to pay from income or assets
- Does not prescribe UW standards
- Provides a presumption of compliance

# Higher-Priced Loans

## *Consideration of repayment ability*

- Creditors must verify income or assets they rely on
  - Third-party document
  - Limited defense
- Creditors must consider and verify current obligations
  - May rely on credit report

# Higher-Priced Loans

## *Presumption of compliance*

- Verify income or assets relied on & current obligations
- Use highest scheduled payment for first 7 years
- Consider DTI *or* residual income
- Excluded: Neg am; certain balloons
- *Subject to rebuttal*

# Higher-Priced Loans

## *Escrows*

- Mandates escrows on first-lien loans
- Creditor decides whether to permit opt-out
- But opt-out prohibited in first 12 months

# Higher-Priced Loans

## *Prepayment penalties*

- Banned for loans where the payment changes in the first four years of the loan
- Restricted for all other loans (e.g. fixed rate loans)
  - Cannot exceed first 2 years of loan term
  - Cannot be imposed by same creditor or affiliate

# Restrictions on Most Loans

- Prohibits lender or broker from coercing appraiser
- Prohibits servicers from imposing certain unwarranted charges; requires prompt payoff statement

# Disclosure

- Requires advertisements to be accurate and complete; prohibits certain deceptive practices
- Requires loan terms be disclosed three days after application, or before charging a fee (except a fee for credit review)
- *But: Board will propose modifications to disclosure timing to conform to HERA*

# Conclusion

- Effective 10/01/2009 except for escrows
- Board will issue proposed rule on early disclosures to conform to HERA
- Regulation C (HMDA) to be conformed to HOEPA's "higher-priced" loan