

Federal Law Update

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Changes in the Past Year

- Final Appraisal Code of Conduct
 - Recent developments for mortgage brokers
- TILA/HOEPA Regulations
 - Issued last summer and slated to go into effect later this year
- Recent FHA Changes
 - Increased mortgage amounts
 - Changes to the refinance program
 - Non-approved broker fees
 - Co-branded advertising

Appraisal Code of Conduct

- Revised Home Valuation Code of Conduct released by the Federal Housing Finance Agency (“FHFA”) on December 23, 2008
- Applies to mortgage lenders that sell residential mortgage loans to Fannie Mae and Freddie Mac
- Effective date is May 1, 2009

Summary

- History
- Highlights of the Code
- Appraiser Selection – Mortgage Broker Issues
- NAMB Lawsuit

History

- Code first arose in connection with a March 2008 settlement between FHFA, the New York Attorney General, and Fannie Mae and Freddie Mac related to the reform of mortgage lenders' appraisal practices
- Initially proposed sweeping changes to the appraisal process

History

- Code would have prevented lenders from:
 - employing staff appraisers
 - operating their own appraisal management companies and
 - using vendor management companies owned by entities that perform other settlement services (i.e., title insurance)

Highlights of the Code

1. Appraiser Independence
2. Preventing Improper Influence
3. Independent Valuation Protection Institute
4. Quality Control and Certifications

1. Appraiser Independence

- Code forbids any attempt to influence appraisals through coercion, extortion, collusion, compensation, inducement, intimidation, bribery, or in any other manner.
- Provides examples – not an exclusive list – of such coercive activity, including, among other actions:
 - withholding timely payment for appraisal reports;
 - conditioning the payment of appraisal fees on the opinion or valuation to be reached;
 - providing appraisers with stock or other financial or non-financial benefits; and
 - providing an appraiser with a desired value for a subject property (although the appraiser may receive a copy of the sales contract).

1. Appraiser Independence

- Obtaining a second appraisal or AVM in connection with a mortgage transaction is considered coercive unless:
 - lender has a reasonable basis to believe that the initial appraisal was flawed and makes a notation in the loan file regarding its belief; or
 - orders the second appraisal according to written, pre-established guidelines
- Must select the most reliable appraisal, rather than the appraisal that states the highest value

2. Preventing Improper Influence

- Code continues to prohibit a lender from utilizing an appraisal report prepared by an appraiser that is employed by or affiliated with the lender
- In a substantial revision to the FHFA's initial proposals, this prohibition will not apply if eight specific guidelines are met. Generally the lender must:
 - institute certain practices to isolate its sale and loan production staff from the appraiser,
 - not attempt to influence the appraiser's valuation,
 - develop written policies to implement the Code, and
 - subject its appraisal functions to an external audit

2. Preventing Improper Influence

- Code continues to prohibit a vendor management company owned or affiliated with a settlement service provider from performing appraisals for lenders.
- Code now provides a two-part exception to allow settlement service provider-owned vendor management companies to continue performing appraisals, if the vendor management company:
 - has adopted written policies and procedures implementing the Code; and
 - recognizes that once an Independent Valuation Protection Institute (“Institute”) is established, it will receive complaints regarding noncompliance with the Code

3. Independent Valuation Protection Institute

- Code creates the Institute to establish a telephone hotline and email address to accept complaints from appraisers and others regarding non-compliance with the Code
- Will review and report complaints to Fannie Mae and Freddie Mac
- Will publish and promote best practices for independent valuation
- Code obligates lenders to report appraisers who violate applicable laws to state agencies

4. Quality Control and Certifications

- Lenders are required to perform quality control tests on a randomly selected 10 percent sample of appraisals or valuations used
 - Must report adverse findings to Fannie Mae or Freddie Mac
- Must certify that appraisal reports are obtained in compliance with the Code

Appraiser Engagement - Mortgage Broker Issues

- Revised Code authorizes only lenders or entities acting on the lender's behalf (appraisal management companies) to select, retain, and pay appraisers
- The lender is prohibited from accepting any appraisal report completed by an appraiser who was selected, retained or compensated by any other third party, including mortgage brokers and real estate agents.

NAMB Lawsuit

- Filed complaint against FHFA on February 23, 2009
- Challenges the final Code as placing mortgage brokers in a significant and permanent competitive disadvantage that would impede competition in the mortgage lending industry
- Requests a preliminary and permanent injunction of FHFA's enforcement of the Code

NAMB Complaint Arguments

- Code goes beyond the authority of the FHFA to regulate Fannie Mae and Freddie Mac
- FHFA did not comply with the Administrative Procedures Act in promulgating the Code
- Code constitutes an improper delegation of the FHFA's federal regulatory authority to the New York Attorney General (where the Code began)
- Arbitrary and capricious – contrary to the intent of Congress and directly conflicts with regulations, policies and guidelines regarding appraisals that are already in place

TILA/HOEPA Regulations

- Adopted on July 14, 2008
- Amends Regulation Z, implementing the Truth in Lending Act (TILA) and the Home Ownership and Equity Protection Act (HOEPA)
- Effective October 1, 2009
 - Except for certain escrow requirements, which will be phased in throughout 2010

Summary

- Creates a category of “higher-priced mortgage loans” subject to new requirements
 - Intended to cover sub-prime loans not otherwise covered by the HOEPA “high-cost” provisions
 - The portion of loans between “prime” and HOEPA “high-cost”
- New requirements for all closed-end mortgage transactions
- New advertising requirements

Mortgage Broker Disclosure – Proposed Rule

- Had proposed a yield-spread premium disclosure in proposed rule
- Would have prohibited a creditor from paying a mortgage broker any amount that exceeded the total compensation reflected in a written agreement between the consumer and the broker

Mortgage Broker Disclosure – Final Rule

- Board dropped the provision entirely in the final regulation
- Decided it would result in consumer confusion about the broker's role and compensation
- May Revisit this Issue

Higher Priced Loan Requirements

1. What is a “higher priced loan”?
2. Higher Priced Loan Requirements
 - Ability to Repay Analysis
 - Ban on Prepayment Penalties
 - Escrow Account Requirement

“Higher Priced Loan”

- Closed-end, consumer credit transactions secured by the consumer’s principal dwelling
- First-lien loans – APR is 1.5 percentage points above Freddie Mac’s “average prime offer rate” as of the rate lock date
- Subordinate-lien loans – APR is 3.5 percentage points above the “average prime offer rate”
- Board intends to publish each week its average prime offer rates
- Will rely on the “average prime offer rate” from Freddie Mac’s Primary Mortgage Market Survey (PMMS)

1. Ability to Repay

- Prohibits a lender from making a loan without regard to a borrower's ability to repay the loan from verified income and assets other than the home's value
- Documentation – creditor must verify the income and assets used to assess repayment ability

1. Ability to Repay

- “Safe-harbor” presumption of compliance if the creditor:
 1. Verifies and documents the borrower’s repayment ability
 2. Determines the consumer’s repayment ability using the largest payment of principal and interest scheduled in the first seven years
 3. Assesses the consumer’s repayment ability taking into account either the total debt obligation to income (“DTI”) or the income the consumer will have after paying debt obligations

- Presumption can be rebutted

2. Ban on Prepayment Penalties

- Higher-priced loans may not include prepayment penalties if the payment can change during the loan's first four years
- In all other higher-priced loans, prepayment penalty period (1) cannot last for more than two years and (2) may not be imposed on a "same creditor refinance"

3. Escrow Account Requirement

- Must establish an escrow account for the payment of property taxes and homeowners' insurance for first-lien higher-priced loans
- Can offer the borrower the opportunity to cancel the escrow account after one year

Closed-End Residential Mortgage Provisions

- Applies to all closed-end mortgage loans secured by a consumer's principal dwelling
- Open-end home equity plans are excluded
- Summary:
 1. Prohibition on appraiser coercion
 2. Prohibition on servicer practices
 3. Earlier disclosures

1. Prohibition on Appraiser Coercion

- Prohibits creditors, mortgage brokers, and their affiliates from coercing, influencing, or otherwise encouraging appraisers to misstate or misrepresent the value of a consumer's principal dwelling

- Prohibits creditors from extending credit if the creditor knew of a violation – i.e., appraiser encouraged by a mortgage broker or affiliate to misstate or misrepresent value – unless:
 - creditor acts with reasonable diligence to determine the appraisal was accurate or
 - extends credit based on a separate, untainted appraisal

2. Prohibition on Servicer Practices

- Failing to credit a consumer's periodic payment as of the date received
- “Pyramid” late fees
- Failing to provide an accurate payoff statement within reasonable time after request

3. Earlier Disclosures

- Expands the requirement that a creditor must provide a consumer with an early GFE disclosure under TILA to mortgage refinancings, closed-end home equity loans, and reverse mortgages
- Must be provided within three days after a consumer applies for the loan
- Must include total payments, finance charge, amount financed and APR

Advertising Requirements

- Amends advertising rules for virtually all residential mortgage loans – closed-end mortgages and open-end home equity plans
- Must disclose all rates or payments that will apply over the term of the loan with equal prominence in close proximity to the advertised rate/payment
- Required whenever rate or payment is included in the advertisement
- Bans certain deceptive or misleading practices

Recent FHA Changes

1. Increased Maximum Loan Limits
2. Refinance Transactions
3. Non-Approved Broker Fees
4. Co-Branded Marketing

1. Increased Maximum Loan Limits

- Mortgagee Letter 2009-07
- Loan limit increases are effective for those loans for which credit is approved in calendar year 2009 and will remain in effect until December 31, 2009

1. Increased Maximum Loan Limits

- “Floor” limits remain at 65% of the conforming loan limit, or \$271,050 for single-family properties
- “Ceiling” limits at 175% of the conforming loan limit, or \$729,750
- HUD provided a list of those geographic areas above the ceiling and between the floor and the ceiling:
<https://entp.hud.gov/idapp/html/hicostlook.cfm>

1. Increased Maximum Loan Limits

- FHA loan limit for Home Equity Conversion Mortgage (“HECM”) loans also was increased from \$417,000 to \$625,500 (from 100% to 150% of the conforming loan limit).
- Applies to HECM loans closed on or after February 24, 2009

2. Refinance Transactions

- New maximum mortgage calculation – for case numbers assigned on and after January 1, 2009
 - Maximum LTV for most refinance loans is 97.75%
 - Maximum LTV for cash-out refinances still 85% or 95%
- Provides a chart comparing the different refinance types
- Letter provides guidance on how to calculate the loan amounts, what can be included in the existing debt, and additional underwriting criteria

2. Cash-Out Refinance Transactions

- LTV still limited to 85% when the loan amount will exceed \$417,000
- Second Appraisal required for cash-out refinances where LTV exceeds 85% - regardless of loan amount or declining area
- Cash-out refinances will be “over-selected” for post-endorsement technical reviews

3. Non-Approved Broker Fees

- An FHA-approved entity must perform all loan origination activities
- Mortgagee Letter 08-17 lists particular origination functions that a non-approved broker may not provide
 - Includes taking the loan application, collecting information or ordering verifications, and providing disclosures

3. Non-Approved Broker Fees

- RESPA requires that mortgage brokers perform certain services, including taking the loan application, to receive compensation from a lender in all loans, including FHA transactions
- RESPA also prohibits the payment of duplicative fees

3. Non-Approved Broker Fees

- Section 203.27 – “Nothing in [Section 203.27] will be construed as prohibiting the mortgagor from dealing through a broker who does not represent the mortgagee, if he prefers to do so, and paying such compensation as is satisfactory to the mortgagor in order to obtain mortgage financing.”
- Permits a borrower to engage a non-approved broker to assist the borrower in obtaining mortgage financing

3. Non-Approved Broker Fees

- Mortgagee Letter 08-17 lists the “counseling”-type servicers non-approved brokers may provide:
 - Educating prospective borrowers in the home buying and financing process
 - Advising the borrower about different types of loan products available
 - Demonstrating how closing costs and monthly payment could vary under each product

- Counseling services must be meaningful and not constitute “steering”

3. Non-Approved Broker Fees

- Must represent the fair market value of the consulting services provided
- Must be paid directly from the borrower's available assets
- Must be disclosed in the 800 series of the HUD-1 Settlement Statement as a broker consulting fee
- FHA-approved originator must provide a copy of the contract between the non-approved broker and the borrower in the case binder submitted for FHA insurance endorsement

4. Co-Branded Outreach Materials

- FHA has developed a series of education and outreach flyers for lenders, real estate professionals, mortgage brokers and housing counselors
- Co-brand/market to prospective customers
- Will be available on www.fha.gov