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Legislative Bulletin……..……May 6, 2009

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Take-Away Points

--***Discouragement of Lending and Investing.*** The bill's numerous and multi-layered regulations on mortgage lenders could discourage some lenders from offering anything but the least risky, most secure mortgages.

--***Intrusion into the Private Market.*** The bill would prohibit a variety of legitimate private-market business practices for lenders and would thus amount to an unwelcome federal micromanagement of private markets and private lives. Such intrusion could yield *fewer* loan choices for consumers.

--***Definitional Uncertainty.*** The bill would create numerous federal duties and related liabilities from loan originators that are somewhat subjective, yet would leave the bulk of the operational definitions (such as "appropriate," "ability to repay," and "net tangible benefit" and their related terms) undefined, vaguely defined, or to be defined by regulators sometime in the future.

--***Excessive Liability and New Lawsuits.*** The bill would make creditors liable for compliance with the bill's numerous requirements, with a liability of three times the total amount of "direct and indirect compensation or gain accruing" in connection with a violation.

--***Legal Assistance Slush Fund.*** The bill creates a new $35 million a year program to provide foreclosure legal assistance to low- and moderate-income homeowners.

For more details, see below.

H.R. 1728—Mortgage Reform and Anti-Predatory Lending Act (*Miller, D-NC*)

Order of Business: The House is scheduled to begin consideration of H.R. 1728, the Mortgage Reform and Anti-Predatory Lending Act on Wednesday, May 6, 2009 under a general debate rule. The rule waives all points of order against consider of the bill (except those for PAYGO

and earmarks) and provides one hour of debate. The RSC will summarize any amendments made in order under a separate rule governing amendments in a separate document.

Summary: Highlights of the legislation by title are as follows:

Title I—Residential Mortgage Loan Origination Standards

New Regulations on Mortgage Industry: The legislation requires each mortgage originator to be subject to a "federal duty of care" standard requiring the entity to, among other things:

- be registered and licensed as a mortgage originator;
- present the consumer with a range of loan products;
- make "full, complete, and timely" disclosures to each consumer of the comparative cost and benefits of each residential mortgage loan product offered, the nature of the originator's relationship to the consumer, and any relevant conflict of interest;
- certify to the creditor that the mortgage originator has fulfilled all requirements applicable to the originator (under this provision of the bill);

The legislation gives the federal banking agencies the authority to prescribe regulations that the regulators determine is appropriate to meet the purposes of this subsection.

Prohibition on Steering Incentives: The legislation requires that for any mortgage loan, the total amount of direct and indirect compensation from all sources permitted to a mortgage originator may not vary based on the terms of the loan. The legislation gives the federal banking agencies authority to issue regulations that:

- Prohibit mortgage originators from steering any consumer to a residential mortgage loan that the consumer lacks a reasonable ability to repay, does not provide the consumer with a net tangible benefit, or has "predatory characteristics or effects."
- Prohibit mortgage originators from steering any consumer from a residential mortgage loan that is qualified to one that is not qualified.
- Prohibit abusive or unfair lending practices that "promote disparities among consumers of equal credit worthiness but of different race, ethnicity, gender, or age"; and
- Prohibit mortgage originators from assessing excessive points and fees to a consumer based on the consumer's decision to finance all or part of the payment through the rate for such points and fees.

Liability: The bill creates a federal cause of action (i.e. allowable lawsuits) for a mortgage originator's failure to comply with legislation. The legislation sets a maximum liability of the greater of actual damages or three times the amount of direct and indirect gain to the originator.

Discretionary Regulatory Authority: The legislation gives the federal banking agencies the authority to issue regulations that prohibit acts or practices relating to residential mortgage loans that the agencies find to be "abusive, unfair, deceptive, predatory, inconsistent with reasonable underwriting standards, necessary or proper to effectuate the purposes of this section and section 129C." The legislation also requires the Secretary of HUD and the Board of Governors to,

within six months of enactment, issue regulations "providing for compatible disclosures for borrowers to receive at the time of mortgage application and at the time of closing."

Title II—Minimum Standards for Mortgages

Ability to Repay: The legislation requires federal banking agencies to issue regulations prohibiting a creditor from making a residential mortgage loan, unless a determination is made by the creditor (based on verified and documented information) that the consumer has "a reasonable ability to repay the loan."

Multiple Loans: H.R. 1728 requires a creditor to make a reasonable and good faith determination that a consumer has a reasonable ability to repay the combined payments of all loans if the consumer has more than one loan.

Net Tangible Benefit for Refinancing of Residential Mortgage Loans: The legislation prohibits a creditor from refinancing a loan unless "the creditor reasonably and in good faith determines" that the refinanced loan will provide a net tangible benefit to the consumer. The legislation also requires the federal banking agencies to prescribe regulations defining the term "net tangible benefit."

Safe Harbor: The legislation would allow certain loans to be classified as safe harbor loans for purposes of this legislation. A safe harbor loan would be presumed to meet the standards of the legislation. A safe harbor loan would have to meet certain conditions, including:

- Not have deferred payments.
- Not cause a negative amoritization.
- Not have a "balloon payment" (where the loan for one month is twice as large as the average monthly payment to date).
- Not exceed prime interest rates by 1.5 percentage points (in the case of a first lien) or 2.5 percentage points (in the case of a subordinate loan).
- Income and financial resources of the borrower are verified and documented.

However, the legislation also gives the federal banking agencies the authority to prescribe regulations that add to or subtract from the above criteria.

Liability: The bill provides that a consumer has a cause of action against a creditor for rescission of the loan, and the consumer's costs for a loan, that violates the minimum standards for reasonable ability to repay or net tangible benefits as set forth by regulation.

Effect on State Laws: Explicitly provides that the liability and remedy provisions of this legislation trump any related provisions in state laws. State laws against creditors and other state laws not related to this legislation would not be superseded.

Civil Liability Provisions: The legislation doubles certain civil liability provisions and extends the statute of limitations from one year to three years.

Hybrid Adjustable Rate Mortgages: Requires a creditor to send a written notice, six months before a hybrid rate mortgage is about to reset, that contains information specified in the bill.

Credit Risk Retention: Requires federal banking agencies to prescribe regulations that require creditors (except for loans protected by the bill's safe harbor provision) to retain an economic interest in a material portion (at least 5 percent) of the credit risk for any such loan that the creditor transfers, sells or conveys to a third party.

Legal Assistance for Foreclosure Related Issues: H.R. 1728 creates a new program to provide foreclosure legal assistance to low- and moderate-income homeowners. The legislation authorizes $35 million a year over the FY 2009-2012 period for this program ($140 million total). The reported text includes an amendment offered by Representative Bachmann (R-MN), and accepted by the Democrats on the committee, that would prohibit funding for "any organization which has been indicted for a violation under federal law related to an election for federal office." ACORN would be an example of such an organization. Despite accepting the amendment at mark-up, Chairman Frank now plans to offer an amendment that would undo the effect of the Bachmann amendment.

GAO Report: The legislation requires the Comptroller General to conduct a study to determine the effects of enactment of the legislation, including the effect on the mortgage market and on the ability of prospective homebuyers to obtain financing.

Tenant Protections: The legislation gives a tenant (except under certain exceptions spelled out in the bill) the right to stay through the end of a lease in the case of any foreclosure.

Title III—High-Cost Mortgages

In response to reports of predatory lending practices in home equity lending in the early 1990s, Congress enacted the Home Ownership and Equity Protection Act (HOEPA) in 1994, which covers home equity loans but not purchase-money mortgages (mortgages in which the buyer borrows money from the seller, rather than from a bank). Loans are classified as "high-cost home loans" under HOEPA because of their high annual percentage rates (APRs) or because their points and fees trigger certain prohibitions and/or disclosures. Under HOEPA, the Federal Reserve Board has the authority to prevent "unfair and deceptive" lending by writing regulations governing state and lenders.

- Adds purchase-money mortgages and open-end loans (revolving lines of credit that are always open up to a limit) to HOEPA.

- Codifies the current APR trigger at 8% above comparable Treasuries for first mortgages and comparable Treasuries (unless the loan is less than $50,000 and for a personal property).

- Lowers the points-and-fees trigger from 8% to 5% for most loans (except those secured by personal property).

- Prohibits balloon payments (a lump-sum payment due at the end of a mortgage) on HOEPA loans, unless the payment schedule is adjusted to the seasonal or irregular income of the consumer.

- Allows creditors to correct non-bona fide errors within 30 days of the loan closing and prior to the institution of any action (60 days for bona fide error).

- Directs the Federal Reserve Board to implement regulations under this title within six months of enactment and deems the amendments made by this title effective upon enactment (and applicable to high-cost mortgages consummated on or after that date).

Title IV—Office of Housing Counseling

- Establishes the Office of Housing Counseling under the Office of the HUD Secretary.

- Makes the office responsible for all HUD homeownership and rental housing counseling programs (including matters of refinancing and foreclosure), and for establishing, coordinating, and administering all regulations, requirements, standards, and performance measures under the programs that relate to housing counseling, homeownership counseling, mortgage-related counseling, and rental housing counseling.

- Authorizes $3 million for each of fiscal years 2009-2011 for a *national public service multimedia campaign* to make "potentially vulnerable" consumers (including the elderly, the poor, people who don't know English very well, people facing mortgage foreclosure, and people considering a subprime mortgage) aware of the existence and benefits of homeownership counseling.

- Directs the Secretary to provide advice and technical assistance to states, units of local government, and non-profit organizations on how they can best educate people about mortgages, refinancing, home equity loans, and home repair loans.

- Directs the Secretary to make grants for homeownership or rental counseling to states, units of local government, and non-profit organizations, subject to standards and guidelines for assistance eligibility created by the Secretary.

- Authorizes $180 million over four years for the operations of the Office of Housing Counseling, homeownership and rental counseling assistance, and other programs required by this title.

- Instructs the Secretary to prepare a booklet at least once every five years to help consumers applying for federally related mortgage loans to understand the nature and costs of real estate settlement services (such as balloon payments, prepayment penalties, variable interest rates, escrow accounts, home inspections, consumer rights, etc.). The booklet would have to be produced "in various languages and cultural styles, as the Secretary determines to be appropriate, so that the booklet is understandable and accessible to homebuyers in different ethnic and cultural backgrounds."

Title V—Mortgage Servicing

Escrow Accounts: The bill requires higher-cost and subprime loans to have an escrow account established at the time the loan is established to taxes and hazard insurance, among other things. The legislation would require, at the time a loan is consummated, the consumer to have received written disclosures advising them of the responsibilities of the consumer and implications for the consumer in the absence of any such account.

Title VI—Appraisal Activities

- Requires a physical property visit, for an appraisal of a property, in the case of a subprime mortgage.
- Requires the Federal Reserve, the Comptroller of the Currency, the Director of the Office of Thrift Supervision, and the Federal Deposit Insurance Corporation, to issue regulations intended to prohibit unfair and deceptive practices and acts relating to certain consumer credit transactions.
- Requires the Comptroller General to conduct a comprehensive study within 18 months of enactment of this Act on possible improvements in the appraisal process.
- Requires each creditor to furnish an applicant a copy of any written appraisals within 3 days of a closing.
- Requires the fees paid by the appraiser, and the administration fee charged by the company, be disclosed to the consumer.

Title VII—Sense of Congress on GSEs

Sense of Congress: Expresses the Sense of the Congress that: "efforts to enhance by the protection, limitation, and regulation of the terms of residential mortgage credit and the practices related to such credit and the practices related to such credit would be incomplete without enactment of meaningful structural reforms of Fannie Mae and Freddie Mac."

Committee Action: The legislation was introduced on March 26, 2009 and referred to the Financial Services Committee, which, on April 29, 2009, marked up and ordered the bill reported (as amended) to the full House by a vote of 49-21.

The House considered similar legislation, though with many differences, in the 110th Congress (H.R. 3915). It passed the House by a vote of 291-127. Ranking Member Bachus is opposed to H.R. 1728.

Potential Conservative Concerns: Many conservatives have expressed concerns about H.R. 1728. Some of these concerns are as follows:

- Discouragement of Lending and Investing. The bill's numerous and multi-layered regulations on mortgage lenders could discourage some lenders from offering anything but the least risky, most secure prime mortgages. Some lenders may not want to take the chance with subprime products and risk being held liable for imperfections in the

borrower's financial situation, yet subprime loans are many people's financial foot in the door to a life of homeownership. The bill discounts the notion that businesses and individuals change their behavior when faced with new, burdensome regulations. As Stuart Saft wrote in *The Wall Street Journal* in 2007, "Capital, like water, seeks its own level. If the people who buy the securitized loans, and the institutions who invest in pools of mortgage loans, are no longer secure in being able to get their money back or the interest paid, they will find other investments, and countries, where they can."

- Intrusion into the Private Market. The bill would prohibit a variety of legitimate private-market business practices for lenders and would thus amount to an unwelcome federal micromanagement of private markets and private lives. Such intrusion could yield *fewer* loan choices for consumers.

- Definitional Uncertainty. The bill would create numerous federal duties and related liabilities for loan originators that are somewhat subjective, yet would leave the bulk of the operational definitions (such as "appropriate," "ability to repay," and "net tangible benefit" and their related terms) undefined, vaguely defined, or to be defined by regulators sometime in the future.

- Excessive Liability and New Lawsuits. The bill would make creditors liable for compliance with the bill's numerous requirements, with a liability of three times the total amount of "direct and indirect compensation or gain accruing" in connection with a violation.

- Preemption of State Laws. The bill would preempt state laws in several respects. For example, the bill would preempt state foreclosure laws that allow a foreclosing creditor to evict a renter. This provision could greatly disrupt an investor's ability to transfer a property after foreclosure, possibly yielding higher interest rates, especially on higher risk loans, to compensate for the potential of increased losses in the case of a foreclosure.

Administration Position: A Statement of Administration Policy (SAP) for H.R. 1728 is not available at press time.

Cost to Taxpayers: CBO estimates that H.R. 1728, as reported from the Financial Services Committee, would authorize appropriations of $419 million over the FY2009-FY2014 period. The bill would also increase mandatory spending by $13 million over five years. Lastly, the bill would increase revenues by $13 million over five years.

Does the Bill Expand the Size and Scope of the Federal Government?: Yes, the bill imposes many new regulations on the private-sector and creates new programs.

Does the Bill Contain Any New State-Government, Local-Government, or Private-Sector Mandates?: Yes, the bill is chock full of intergovernmental and private-sector mandates. In the score for the legislation, CBO states that it cannot determine whether these violations exceed the thresholds established under UMRA.

Does the Bill Comply with House Rules Regarding Earmarks/Limited Tax Benefits/Limited Tariff Benefits?: The Financial Services Committee, in House Report 110-091, asserts that, "H.R. 1728 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9 of rule XXI."

Constitutional Authority: The Financial Services Committee, in House Report 111-091, cites constitutional authority in Article I, Section 8, Clauses 1 and 3 (the congressional powers to provide for the general welfare and to regulate interstate commerce, respectively).

Outside Groups: The Mortgage Bankers Association and the American Bankers Association both have concerns with provisions in the bill. The National Realtors Association urges a "yes" vote.

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