

## A Mortgage and Consumer Finance Law Update

08/04/09

### Federal Reserve Board Proposes More Changes to Truth-in-Lending

On July 23, 2009, the Federal Reserve Board (the "Board") published proposed rules that will make more sweeping changes to Truth-in-Lending's ("TILA") closed-end residential loan and dwelling-secured open-end credit plan rules. The changes would impact the disclosures given at all stages of the loan process. Comments are due by November 27, 2009.

#### Closed-End Residential Loan Disclosures

##### Disclosures at Application

Under the proposed rules, creditors would be required to provide two new Board publications entitled "Key Questions About Your Mortgage Application" and "Fixed vs. Adjustable Rate Mortgages." These publications would replace the current Consumer Handbook on Adjustable Rate Mortgages ("CHARM"). They would be provided on all closed-end mortgages and before the earlier of: (1) submission of the application, or (2) payment of a non-refundable fee. Creditors would continue to provide Adjustable Rate Mortgage ("ARM") program disclosures on adjustable rate loans, but the current program disclosure form would be replaced by disclosures in a tabular and question and answer format.

##### Disclosures Within Three Business Days After Application

The proposed rules would make several changes to the format and content of the 3 day disclosures:

- The Annual Percentage Rate ("APR") would include charges by third parties if the creditor requires the use of a third party (even if the consumer selects the third party) or if the creditor retains a portion of the fee. The Board acknowledges that this change means that more loans will be subject to the Home Ownership and Equity Protection Act ("HOEPA") and state predatory lending laws.
- "Finance Charge" would be replaced with "Interest and Settlement Charges."
- The APR would have to be disclosed in 16 point font and in close proximity to a graph comparing the APR to the HOEPA average prime offer rate for borrowers with excellent credit and the HOEPA threshold for higher priced mortgages.
- The current payment schedule disclosure would be replaced with a tabular disclosure of the interest rate and monthly payment (including principal, interest, escrows and

mortgage insurance). In the case of ARMs and step rate loans, creditors would be required to disclose the initial, first adjusted and maximum interest rate and payment.

- Other key terms (*e.g.*, loan amount, loan term, loan type, etc.) would be provided in tabular format, along with a question and answer document called "Key Questions About Risk."

#### Disclosures Three Days Prior to Consummation

The Board is requesting comment on two different alternatives. The first approach would require that the final TILA disclosures be provided three business days prior to consummation even if the earlier disclosures remain accurate. Under the second alternative, the creditor would redisclose but would only have to wait three business days to close if the APR exceeded the applicable tolerance or the creditor added an adjustable rate feature.

#### Disclosures After Closing

ARM rate adjustments would be provided at least 60 days before the new payment is due. In the case of a loan with negative amortization, statements would have to be provided at least 15 days before the payment due date. They would also have to contain a table comparing each payment option. Creditors would also have to provide at least 45 days advance notice of forced placed insurance.

#### Mortgage Broker and Originator Compensation

The Board is proposing to prohibit the payments of yield spread premiums to brokers and overages to employees. In addition, originators could no longer be compensated based on credit terms or conditions.

#### **Disclosures on Home Equity Lines of Credit**

##### Early Disclosures

The application disclosures required under current Regulation Z would be replaced with transaction-specific disclosures to be given within three business days of the application. Several additional disclosures would be required that are not contained in the current initial terms disclosure and the disclosures would have to be in a tabular format.

##### Account Opening Disclosures and Periodic Statements

The account opening disclosures would be revised to require that certain costs and terms be listed in a table. In addition, the proposed rule would more precisely identify the charges that creditors must disclose in writing at account opening. With respect to periodic statements, creditors would no longer need to disclose the Effective (a.k.a., Historical) APR, costs would be disclosed as "interest" and "fees" instead of "finance charges" and "other charges." The interest and fees would be grouped together and creditors would show totals for the billing period and year to date. All of these changes would be consistent with the Board's changes to the other

open-end disclosure rules that take effect on July 1, 2010.

### Change in Terms Notices

Change in terms notices would have to be provided at least 45 days in advance of the change instead of the current 15 days. Certain changed terms would have to be provided in a summary table. Again, these changes are consistent with those to the other open-end credit rules that take effect next year.

### Account Termination and Suspension

The Board is also proposing to clarify the limitations on a creditor's ability to suspend and terminate Home Equity Lines of Credit ("HELOCs"):

- Creditors would be prohibited from terminating a HELOC for non payment unless the payment was more than 30 days past due;
- The Board is proposing to add a new "safe harbor" for suspensions based on a "significant" decline in property value. If the combined loan to value at origination was 90 percent or greater, a decline of 5 percent or more would be deemed significant;
- Suspensions for a material change in the borrower's circumstances may be based on credit report information showing late or non payments or public records relating to the consumer's failure to pay other obligations. However, such defaults would need to have occurred within a reasonable time period from the creditor's review. Six months would be a "safe harbor" time period for this purpose; and
- The Board is also proposing that suspension notices contain additional information regarding the consumer's right to request reinstatement.

For more information, please contact the Mortgage and Consumer Finance Law Industry Team at Lane Powell:

206.223.7000 Seattle

503.778.2100 Portland

360.754.6001 Olympia

[MortgageAndFinance@lanepowell.com](mailto:MortgageAndFinance@lanepowell.com)

[www.lanepowell.com](http://www.lanepowell.com)

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