Mortgage Q&A with the Consumer Financial Protection Bureau

Presented by the American Bankers Association
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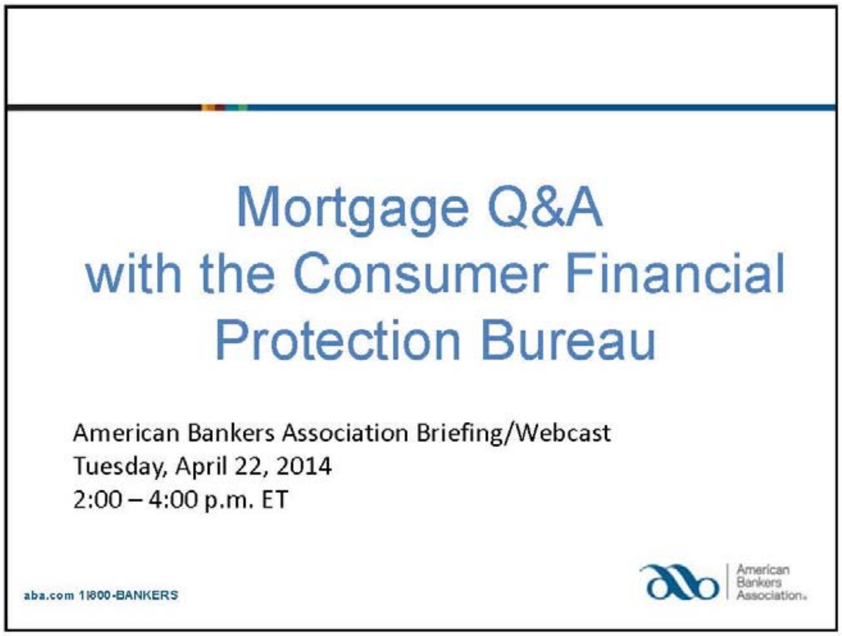
Transcript prepared by BuckleySandler LLP[1]



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And it's my pleasure at this time, to introduce one of our co-moderators for the program, Krista Shonk. Krista is Vice President of Mortgage and Finance and Senior Regulatory Counsel for the

[1] The audio recording and original slides are available for purchase at: http://www.aba.com/Training/teleweb/Pages/tb042214.aspx. The transcript is provided for informational purposes only and does not constitute legal opinions, interpretations, or advice by BuckleySandler. The transcript was prepared from the audio recording provided by the ABA and may have minor inaccuracies due to sound quality. In addition, the transcript has not been reviewed by the CFPB or the ABA for accuracy or completeness. This transcript inserts an image of the slide that corresponds to the discussion, but all insertions are approximate. This transcript also revises citations for consistency with the Code of Federal Regulations (e.g., "1026.32(b)(1)(iii)" instead of "1026.32(b)(1)(3)").

American Bankers Association, and Krista, welcome. I'll pass the microphone over to you at this time.

KRISTA SHONK: Thanks very much, Tim. Good afternoon, everyone. Thanks for participating in today's program to explore some of the commonly asked questions relating to the CFPB's new mortgage rules.

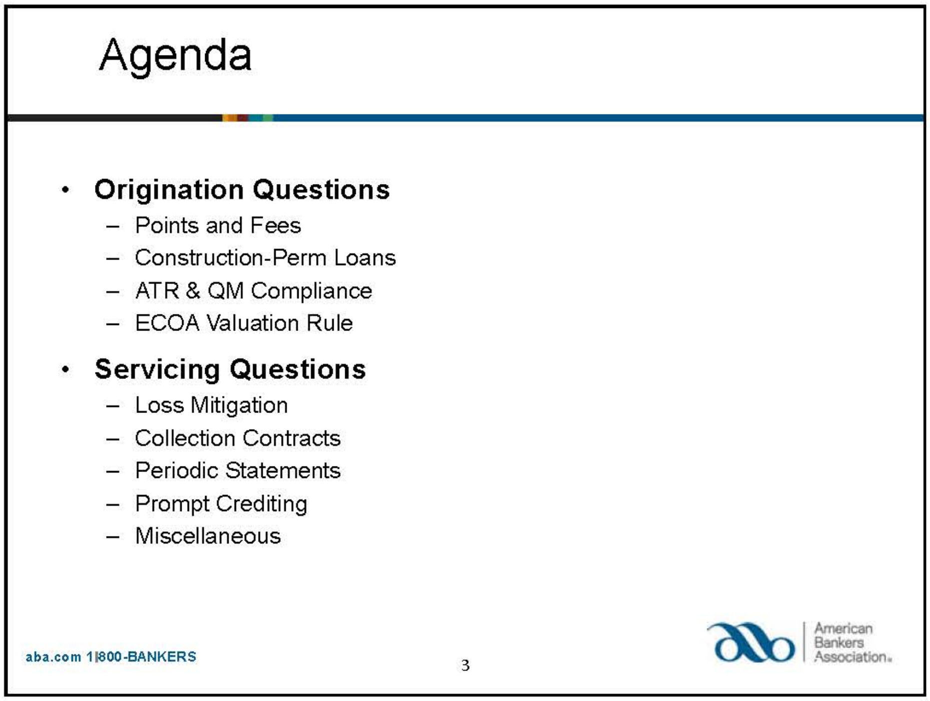
We also appreciate that Nick Hluchyj and Laura Johnson from the CFPB are joining us today. Nick and Laura both serve as senior counsels in the CFPB's Office of Regulation. Their full bios are included in your handout materials, so feel free to read their full biographical information.

Nick and Laura have worked extensively on the new mortgage regulations and we certainly appreciate the time and the preparation that they put into today's call.

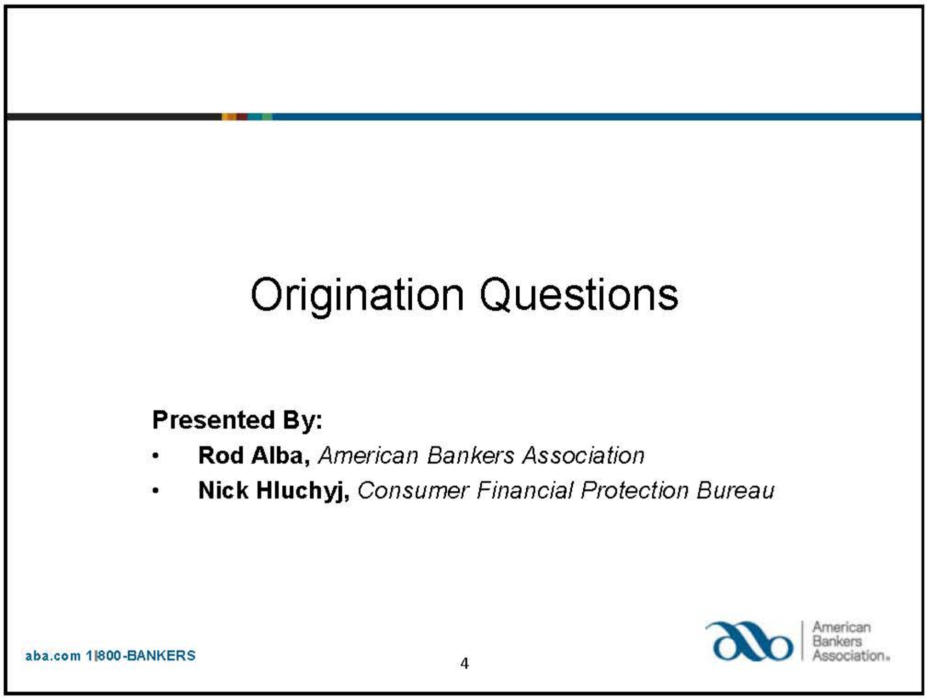
Before we begin the program, just a quick note regarding the material that we will cover today. You may recall that ABA actively solicited questions from our members in preparation for today's program and it really was a case of ask and you shall receive. You all didn't hold back and we certainly have a lot of issues to explore this afternoon. The downside is that we only have two hours today, and that means we will not have time to get to all the questions that you submitted. So we prioritized the, the discussion questions to include those matters that were asked the most frequently and issues that were prioritized by our various banker committees and working groups.

At this time I'll turn the mic over to my colleague, Rod Alba. Many of you know Rod who manages mortgage origination matters for ABA and he's been helping our members work through a lot of the issues tied to the new regulatory structure for mortgage lending. Rod, it's all yours.

ROD ALBA: Thank you, Krista. And I want to thank the CFPB for being here. I will remind everyone again that these questions that we will be presenting today were indeed questions that were crafted and presented by bankers, so they do constitute the most in demand or the most critical inquiries that our bankers had. Nick, would you like to give certain remarks right before we begin with the questions?

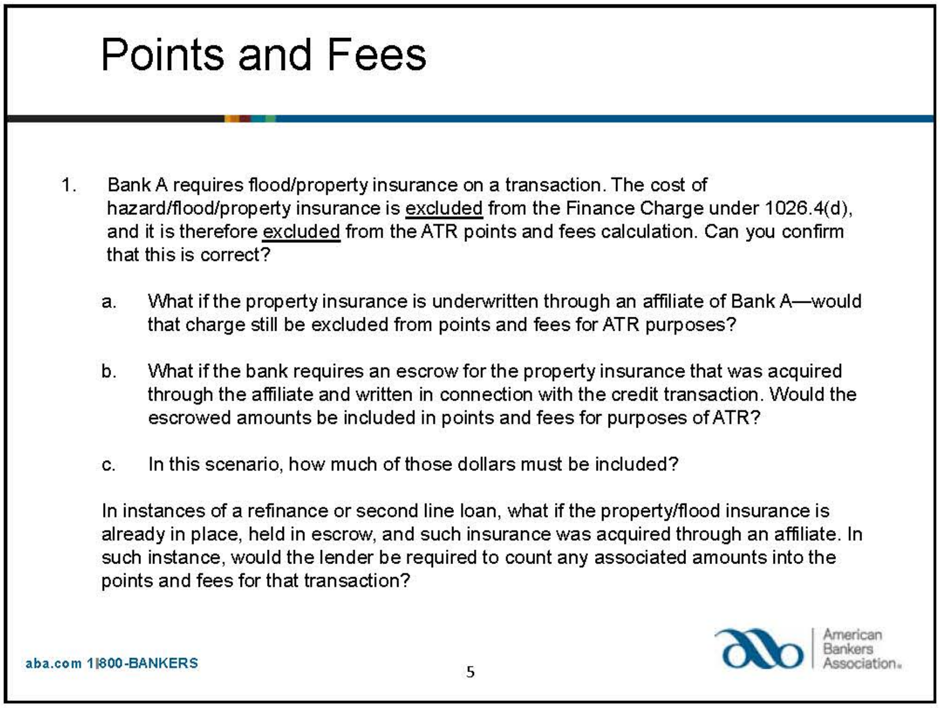


NICK HLUCHYJ: Thank you very much, Rod and thank you, Krista. I'd just like to make a preliminary statement that what we're providing here from the CFPB is in the nature of informal guidance the way we often do when we receive inquiries through our Regs Inquiry Portal and I'd remind everyone listening that you can always do a follow up question or ask additional questions by submitting your questions directly to us and one of our staff will get in touch with you to discuss it.



NICK HLUCHYJ: This is not legally binding and is not intended to be a substitute for the regulations and commentary but it does reflect our best current thinking on the subjects that we will be discussing.

ROD ALBA: Thank you, Nick. With that, let's jump straight into the questions.



ROD ALBA: As you will see in the first slide, which is marked as slide number five, let's begin with points and fees which is an area of much haze with our membership. Let's assume or let's look at Bank A that requires hazard, flood, and property insurance on a transaction. The cost of this insurance is excluded from the finance charge under 1026.4(d). So the statement and the first item that I would like to pose to you, Nick, since it is excluded from the finance charge, is it therefore excluded from the ATR and QM points and fees calculation? Can you confirm that that is correct?

NICK HLUCHYJ: Rod, yes. If it's not included in the finance charge, this particular charge is also not included in points and fees but I'll have to put a caveat on that, generally.

ROD ALBA: So continuing, and that caveat I believe will come up, what if the property insurance is underwritten through an affiliate of Bank A? Would that charge still be excluded from points and fees for ATR and QM purposes?

NICK HLUCHYJ: Yes it is, Rod. Even though it's underwritten through the affiliate or through the bank itself, at this point in the questioning, it would still be excluded.

ROD ALBA: What if the bank requires an escrow for the property insurance that was acquired through the affiliate and written in connection with the credit transaction? Would the escrowed amounts be included in points and fees for purposes of ATR and QM?

NICK HLUCHYJ: At this point, yes. The escrow amounts would be included and here's where it gets a bit complicated, and let me run through the explanation of how this would work.

One of the prongs for the points and fees test is that 1026.32(b)(1)(iii) and that includes fees that would otherwise be excluded from the finance charge under 1026.4(c)(7) unless the fee is not reasonable, is paid through the creditor or an affiliate of the creditor. Now, normally, the hazard insurance payments are, as you noted, not included in the finance charge because they would be excluded under 1026.4(d). However, if they weren't excluded pursuant to that, they would be included but it's very easy to exclude them by giving the required notifications.

Now, there are a number of items listed at 1026.4(c)(7) and romanette (v) lists items that are otherwise not included in the finance charge but which in escrow is established.

That's not a direct quote but it's certainly items that are excluded under escrowed. So here you have a situation where the hazard insurance would be excluded from points and fees but then once it's escrowed, it's captured under (c)(7) fees under romanette (v). And so therefore, it would be included in points and fees.

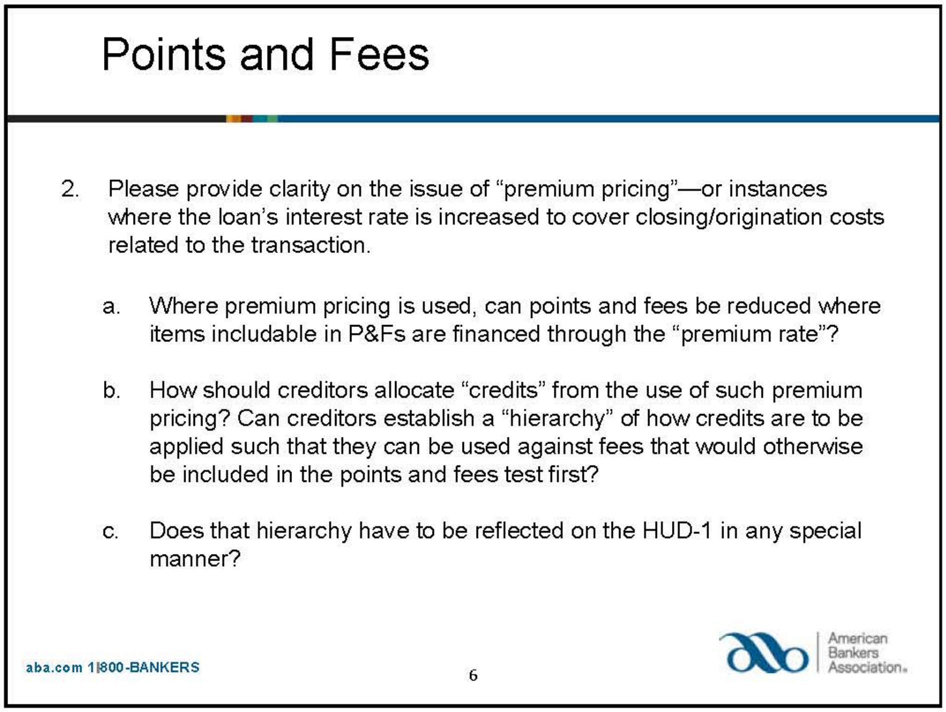
ROD ALBA: Thank you Nick, so in this scenario, how much of those dollars would be included into the points and fees?

NICK HLUCHYJ: Well, and here in the nature of some of the clarifying guidance we've been providing when we've gotten this call through our Regs Inquiry Portal, only the amount that is retained by the creditor or the creditor's affiliate is counted for purposes of points and fees. So that for example, if a portion of the amount is actually passed on to the actual insurer, that amount isn't included in the points and fees. Only the amount that comes through us with the creditor or affiliate is included.

ROD ALBA: So in the last portion of this question, in instances of a refinance or a second lien loan, what if the property/flood insurance is: (1) already in place, (2) held in escrow, and (3) the insurance was acquired through an affiliate? In such an instance, would the lender be required to count any associated amounts into the points and fees for that transaction?

NICK HLUCHYJ: Not unless the, for some reason, the hazard insurance is reissued in connection with the refinancing. If it just continues in steady state as it was, it, just, it carries over. It's not counted as new charge.

ROD ALBA: Thank you.



ROD ALBA: Going on to the next slide, we, I think, our bankers have been asking for clarity on the issue of "premium pricing" in effect, instances where the loan's interest rate in any transaction may be increased to cover closing or origination costs that are related to the transaction. A few questions apply here, the first one, where premium pricing is used, can the QM points and fees be reduced where items are includable in the points and fees are financed through the premium rate?

NICK HLUCHYJ: Yes. They can, and the comment at 1026.32(b)(1)-2.iv specifically states that costs paid by the creditor are not included in points and fees. Now the theory behind this, because this originates with Dodd-Frank and also is related to the previous (c)(7) issue, is that… placing the cost into the interest rate is thought to align the interest of the consumer and the creditor in the long term viability of the loan in a way that charging up-front fees is not. And so you'll notice there are several places within Dodd-Frank where this kind of choice has been made by the legislators. And this is an example of it so that in premium pricing where the cost is rolled up into the interest rates, it's not included in the upfront cost, and that is consistent with the purposes of the Dodd-Frank Act.

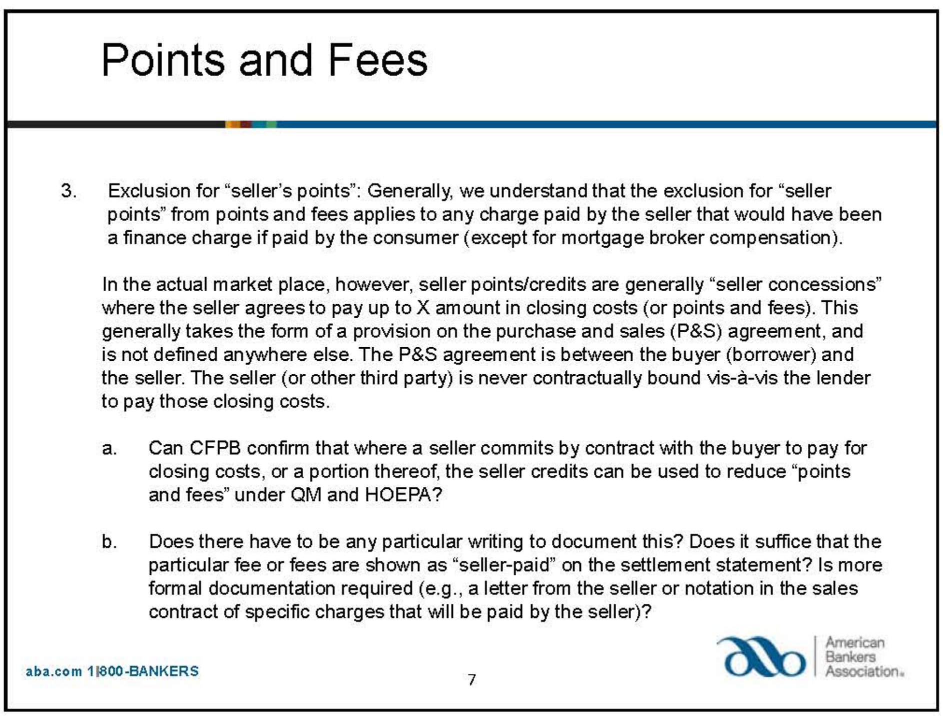
ROD ALBA: So how should creditors allocate these credits from, from the use of premium pricing? Can creditors establish a hierarchy of how credits are to be applied such that they can be used initially against fees that would otherwise be included in the QM points and fees test and perhaps then after that, apply the credit to cancel other fees that are not part of points and fees?

NICK HLUCHYJ: Yes, Rod. It's not so much establishing a hierarchy, something that is automatically executed. There's no reason, I believe, why a creditor couldn't say these are the costs, the upfront costs that we are paying for. And that provides a lot more certainty than having a schedule in place that says allocate them according to "this." One reason for that is the commentary at 1026.4(c)(5)-2, although it deals with seller's points, we'll be discussing that soon too, states that the consumer must no longer be legally obligated on the payment that's made and really the only way of knowing that that's going to be the case is some sort of documentation that actually shows that this cost has been paid and the consumer is no longer liable for it. And so there's, it's in the creditor's interest to establish an actual transaction-by-transaction documentation of what's been paid by the creditor.

ROD ALBA: So I think that goes for the last point, which is, how this gets reflected in the HUD-1. Nick, would you comment on that?

NICK HLUCHYJ: Well, again, I checked, I'm not the HUD-1 expert, but I do know some, and I discussed this question with them prior to coming over. The important point that they want to make is that the HUD-1 is for purposes of disclosure and should not be considered as a way of showing that other requirements under TILA have been met. So the HUD-1 is the HUD-1 to the extent that the creditor is making specific payments that will count towards, or will not count towards, the points and fees. That should be reflected in a separate statement for clarity.

ROD ALBA: Great, so, so thank you Nick.



ROD ALBA: I think that we'll take then, this issue of exactly what needs to be shown with the, with the next slide, slide number seven. Where, as you alluded to, we're going to talk

about the exclusion for seller's, "seller's points." Generally, as we understand the rule, the exclusion for "seller points" from points and fees applies to any charge that is paid by the seller that would have been a finance charge if paid by the consumer and then there is of course the exception for the mortgage broker compensation.

But, you know, I think as we apply this reality, in the actual marketplace, seller points, and, and credits are generally seller concessions where the seller is agreeing to pay up to a particular amount in closing costs or in points and fees. This generally takes a form of the provision on the purchase and sales agreement and is not defined anywhere else, so there is an issue on the contract or who the contract applies to. The P&S agreement is between the buyer, that's generally the borrower, and the seller. The seller or any other third party is never contractually bound vis-a-vis the lender to pay those closing costs. And I think that this brings up some doubts as we read the regulation, so can the CFPB confirm that where a seller commits by contract with the buyer to pay for closing costs or a portion thereof, that the seller credits can be used by the creditor to reduce points and fees under QM and HOEPA.

NICK HLUCHYJ: This is related to our previous question, Rod. Also, I'd like to go back to the beginning of this question where it's, except for mortgage broker compensation, that exception would apply to payments made by the creditor.

So, ordinarily, any fees that would be points and fees, except for mortgage broker compensation, would be excluded for the creditor. The prong that picks up payments to mortgage brokers specifically picks up any payments made directly or indirectly by the creditor to the loan originator.

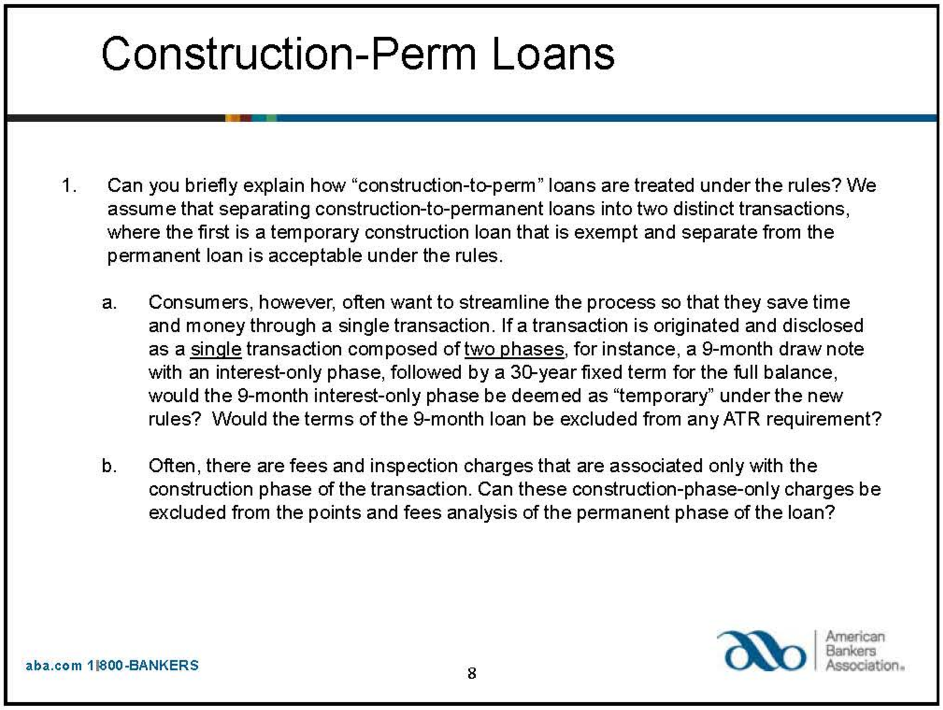
Now, the same issues here come up in the context of payments made by seller. Frequently, the seller would just offer a lump sum to cover, generically, closing costs. And, sometimes at the settlement table, that's when the allocations are being made. The creditor may have a hard time deciphering what's been paid for by the seller and what's been paid for by the consumer, the purchaser. There's commentary specifically on this point, at 1026.32(b)(1)-2 which states that the creditor may rely on a written statement prepared by the seller or other third party for purposes of making the allocations of funds to particular charges.

And, it's once again, probably in the creditor's best interest to have such a statement and maintaining for purposes of demonstrating compliance. Or something specifically provided for in the commentary, it's a good sign post that something indicating compliance with that would survive any examination or subsequent challenge.

ROD ALBA: So, just to address then on the last item, the sufficiency, it would be advisable then to have a writing that is separate from what is noted in the HUD-1 or the settlement statement?

NICK HLUCHYJ: That's correct. A written statement is specifically provided for and would be an indication of compliance with requirements.

ROD ALBA: Thank you, Nick. Going to the next slide, which is slide number eight.



ROD ALBA: Construction-to-perm loans, this certainly has been a concern for our members and I think that we're going to continue to have some questions as we move onto the TILA/RESPA integration project. But at least as it applies to the QM Rules, can you briefly explain how the construction to perm loans are treated under the new rules? We assume that separating construction to permanent loans into two distinct transactions where the first is a temporary construction loan that is exempt and separate from the permanent loan is acceptable under the rules and is explicitly discussed in the rules. Consumers, however, often want to streamline the process so that you don't have two transactions and so that they can save time and money through that one single transaction.

So if a transaction is originated and disclosed as a single transaction composed of two phases so it's not two transactions but it's a single transaction composed of two phases, for instance, we provide in our slide, a 9-month draw note with an interest-only phase, followed by a 30-year fixed term for the full balance, would the 9-month interest-only phase be deemed as "temporary" under the new rules? And, would the terms of the 9-month loan, I guess, or phase of the loan be excluded from any ability to repay requirement?

NICK HLUCHYJ: Yes, Rod. The ATR Regulation at 1026.43(a)(3)(iii), excludes the construction phase of a loan from ATR and QM compliance and the commentary at 43(a)(3)-2 provides that the construction phase and permanent phase may be treated as separate transactions for purposes of making the ATR determination and that the construction loan and the charges associated with the construction loan can be treated separately and apart from the permanent phase of the loan.

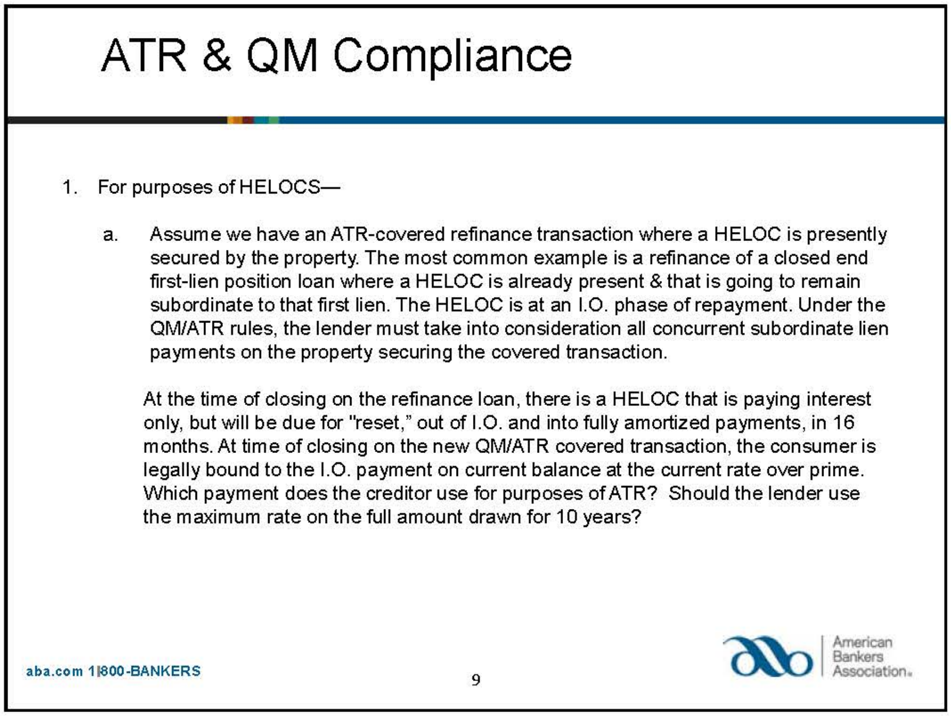
Now there's explicit guidance at 1026.32, the commentary there, is at 32(a)(2)(ii)-1, which speaks of situations where the construction-to-permanent loan is treated either as a single transaction or as two separate transactions because you're also permitted to have separate disclosures for each of those phases, or a single disclosure. It states that when treating them as two separate transactions, the points and fees should be considered to reflect, and the guidance is very broad, the appropriate charges from the permanent phase.

So then the question becomes what are the appropriate charges? And sometimes it's going to be a judgment call, sometimes it's not. Draw fees associated with a construction phase, clearly I wouldn't be counting, because they have nothing to do with the permanent phase of the loan. If there's a single finance charge, for example, there's no guidance other than appropriate charges from the permanent phase. So, again, to the extent that the creditor establishes a written policies and procedures for how such charges might be allocated and they could be based on when these are done, separate transactions, how costs are allocated to construction phase, how costs are allocated to the permanent loan, it may be done perhaps proportionately, but to the extent that the creditor has written policies and procedures and generally follows them in making these determinations, they'll be in a better place with respect to examinations for compliance.

ROD ALBA: So, thank you, Nick. I think that, I think what we're saying certainly is that if there are fees, especially if there are charges, or charges generally, that relate only, only, only to the construction phase of the transaction, we can exclude those from the points and fees analysis that would apply to the permanent loan but the CFPB's going to be on guard that we, lenders, and others don't front load, if you will, the fees and charges to artificially deflate the points and fees calculation for the permanent loan. Is that, perhaps, correctly stated?

NICK HLUCHYJ: That's correct, and that's what we've frequently used in our response to this question when it comes in through our Regs Inquiry Portal. Once again, to the extent that there are separate schedules that deal with construction only loans and permanent only loans, that may be one indicia of showing how one or the other might be front loaded in comparison to those.

ROD ALBA: Thank you.



ROD ALBA: Going onto the next item, we get into HELOCS and balloons. Many of our members, many of our small institutions are really struggling with existing HELOCS and balloon notes that are coming due. The QM and the ATR requirements are placing some, some amount of difficulty, some would say great difficulty, in refinancing some of these transactions, so the following 4 or 5 slides apply to these set of challenges, if you will.

Starting on slide number nine, for purposes of HELOCS, assume that we have an ATR-covered refi transaction where a HELOC is presently secured by the property. Flowing over some of the details that we have in the slide, at the time of closing on the refinance loan, there is a subordinate HELOC that is paying interest only, but will be due for a reset and out of interest only and into fully amortized payments in say 16 months. At the time of closing on the new QM/ATR covered transaction the consumer is legally bound to the interest only payment on current balance at the current rate over prime. So this raises a question again, since the I.O. loan will turn into a fully amortized loan within a specific amount of time, which payment does the creditor use for purposes of ATR? Is it the interest only payment or should the lender use the maximum rate on the full amount drawn for the 10 years in this case?

NICK HLUCHYJ: Well, this is a good question also, Rod. I'm not sure, it's not explicit here, but I'm not sure if the thinking is that this would be considered a simultaneous loan that's considered for payments, but in this instance where you have an existing HELOC, it would be picked up under the 43(c)(2)(vi) current debt obligations test. And the commentary at 43(c)(2)(vi)-1 specifically states that existing mortgages that will not be paid off at or before consummation would be included under the current debt obligations prong. Now, this comment also provides some guidance as to how to consider a known change that's coming. Because if you know it, it states current debt obligations so the thinking would be that it's only what you're paying at the time of consummation. But there is some commentary there that relates to, for example, on debts. If you have a student loan and that's likely to be paid off in the near future, it's not necessary to include that in your consideration.

But then the other side of this two-edged sword, states that, if there's a forbearance or deferral exemption that's going to expire in the future, that may have to be considered depending on how likely it is to affect the consumer's ability to repay in the future.

So, as is frequently the case, with the ability to repay determination, you're making a good faith, a reasonable determination. This is one area the creditor has to examine as to what impact it may have on the particular consumer's ability to repay and the particular transaction. And once again, I'd like to emphasize, it would be good to have policies and procedures in place to address such situations to the extent that they may arise.

ROD ALBA: So, good faith probably would mean that you should look ahead and take into consideration that the payments, the monthly payment for the consumer, is going to jump?

NICK HLUCHYJ: If that seems warranted by the facts and circumstances of the particular case, yes.

ROD ALBA: Okay, going onto slide number ten, for purposes of HELOCS again.

ATR & QM Compliance

1. For purposes of HELOCS (continued)—

   b. Additionally, does Reset/Modification of a HELOC into Closed End Repayments (as set forth in the note) constitute the creation of a new Covered Transaction under QM/ATR?"

   (There is much doubt about whether or not an open-end line of credit (HELOC) can become "a covered transaction under QM/ATR" when it resets, automatically under the terms of the contract, into fully amortizing payments.)

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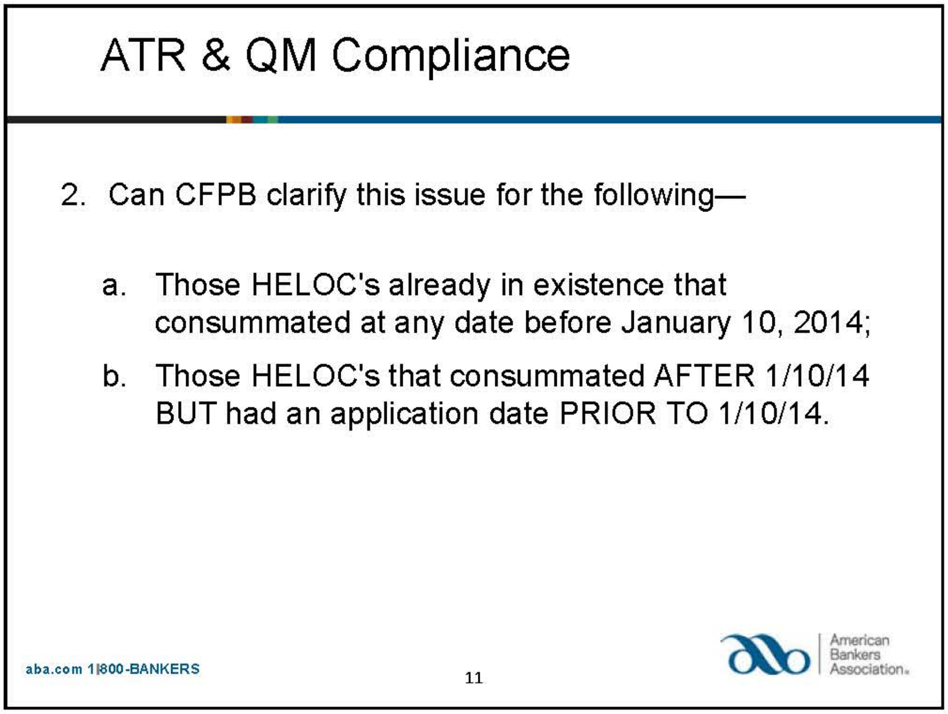
ROD ALBA: Assume, a reset or modification on a HELOC that generally it happens in many transactions, does a reset or modification of a HELOC into a closed-end repayment loan and this, sort of recent modification is set forth in the note, and is set forth in the contract, does this recent re-modification of the HELOC constitute the creation of a new covered transaction under QM/ATR so that you have to engage in that analysis, in the QM analysis when there's a reset under the contract?

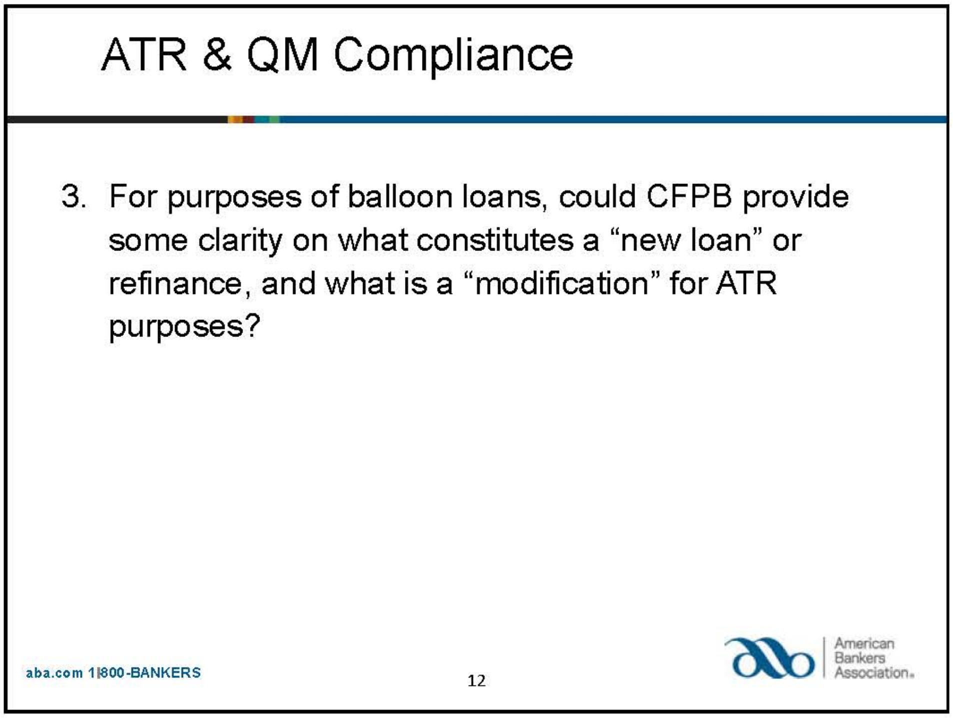
NICK HLUCHYJ: In this instance, HELOCS, as you know, are not subject to the ATR/QM requirements and where a HELOC resets, there does not appear to be the satisfaction of the original obligation and the creation of a new obligation with the same consumer. And therefore, a refinance and the new transaction is not present, and therefore the predetermined, that's already been provided for a reset of the HELOC would not be a new transaction and therefore would not be subject to the ATR/QM requirements at that point.

ROD ALBA: Thank you. That is a much needed clarification, Nick. We appreciate that.



ROD ALBA: On slide number 11, can you, I guess, clarify whether there is going to be special treatment for, and here we're really talking about the dates, and what would be applicable under the different dates given that these, these, the current transactions that may be giving a lot of our banks some trouble were originated before the January 10th effective date. So, can you clarify whether these rules generally apply in the same way for HELOCs already in existence that were consummated at any date before January 10th of 2014 and alternatively, or additionally those HELOCs that consummated after January 10th but had an application date prior to January 10th of 2014?

NICK HLUCHYJ: In either case it would not appear to really matter to the extent that the HELOC resets and is not a refinance. Only new transactions and applications received for new transactions after the January 10th, 2014 date are subject to ATR/QM. And as we discussed on the previous slide, the mere resetting, that's already been part of the contractual obligation, does not create a new transaction.



ROD ALBA: So in the next slide, number 12, this is a question I think that there is clear guidance, or some amount of clear guidance in the regulations, but it is one that we get quite a lot, Nick, and probably the CFPB does too. For purposes of balloon loans, when they come due, certainly in many instances, we would, a consumer will not qualify into a new loan because of the very strict QM requirements for balloons, so for purposes of balloon loans, could CFPB provide some clarity on what constitutes a "new loan" or a refinance, and what is a "modification" for ATR purposes?

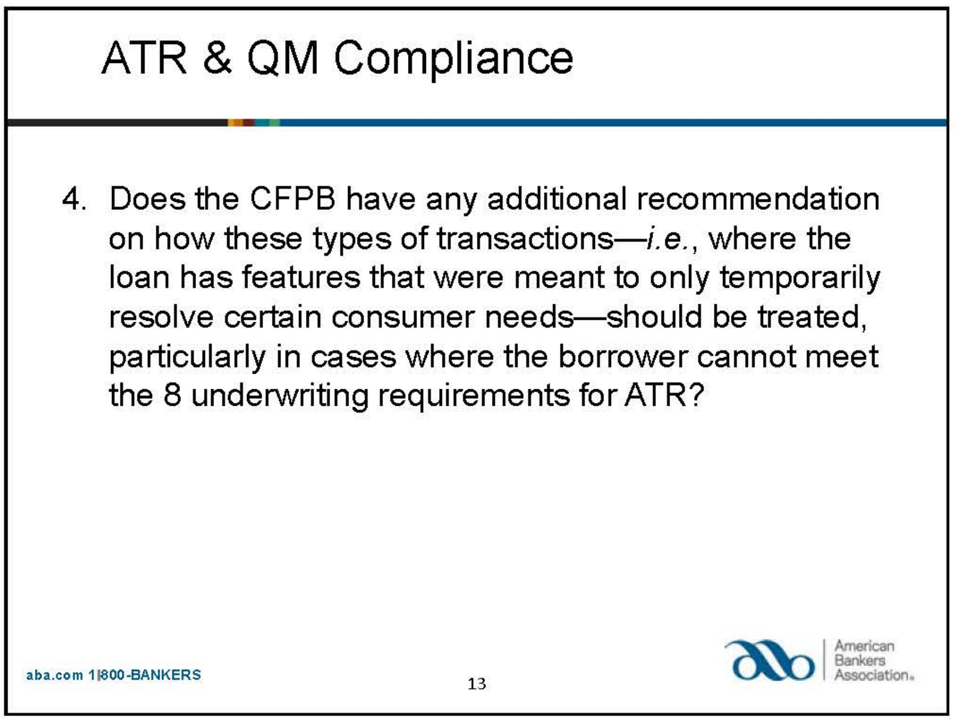
NICK HLUCHYJ: Well, it's possible to clarify what constitutes a refinance. That's clear and that's the satisfaction of the existing obligation and creation of a new obligation with the same consumer. A modification would be something short of that. It would be a change to the existing loan that doesn't create a new obligation. Now, there's a list of transactions that are specifically listed in the regulations at 1026.20(a), which the regulations emphatically states the following shall not be treated as a refinancing, and at least two of the examples there constitutes modifications. The second one, a reduction to annual percentage rates with a corresponding change in the payment schedule, would be a form of modification and to the extent that that's the only action taken, it shall not be treated as a refinancing, therefore, not subject to the ATR/QM requirements.

Also, the fourth item listed, a change in the payment schedule, or change in collateral requirements as a result of consumer's default or delinquency, that also shall not be treated as a refinancing. If you notice, a general statement saying that any modification shall not be treated as a refinancing is not included here. The fact that it's not included does not necessarily lead to the conclusion that it is treated as a refinancing. It just does not get the automatic "shall not be treated as a refinancing" and this becomes a very case specific transaction-by-transaction determination that has to be examined on a case-by-case basis.

ROD ALBA: And, certainly, this is a rule that has existed since TILA was with the Federal Reserve Board, so generally, we would continue to use the legal experience and regulatory experience I guess, that's flowed over from the Board and into the Bureau and I guess my question is, this is not a new provision, Nick?

NICK HLUCHYJ: Correct. Correct. It's a long time requirement.

ROD ALBA: Okay, so in the next slide, and this one is admittedly a broad one and may delve us into policy, but, you know, I think our members want to, as they're looking at the future, and as they're looking at their operations.

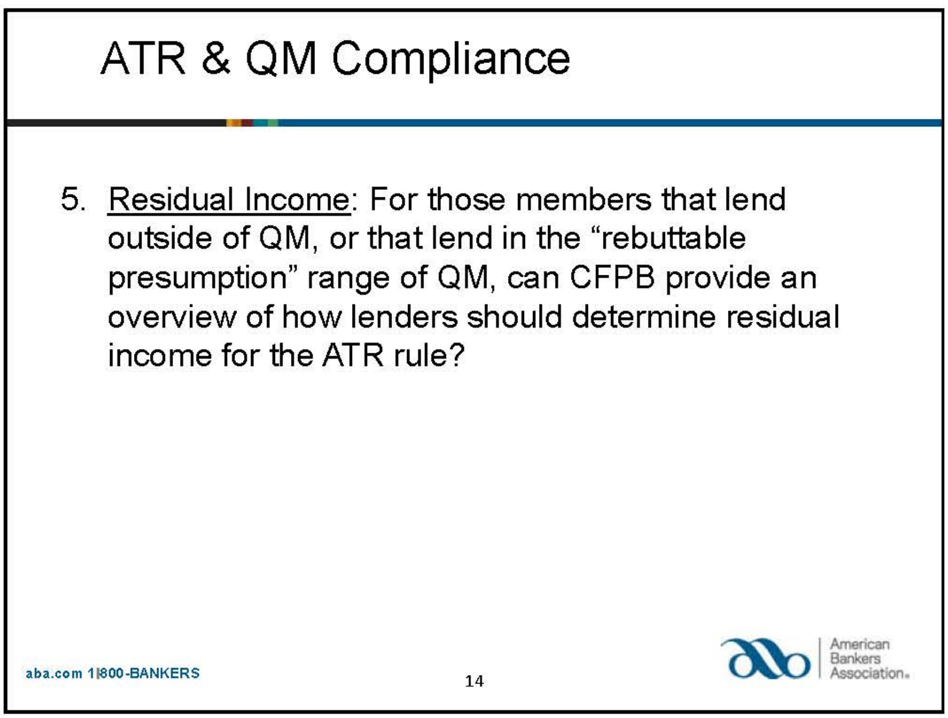


ROD ALBA: Does the CFPB have any additional recommendations on how these types of transactions, in other words, the sort of HELOCs, the balloon loans, where loans have features that were meant to, perhaps temporarily, resolve certain consumer needs were originated, how should we to,Bureau treat those types of transactions in cases where the borrower cannot meet the eight underwriting requirements under ATR? Is it really the only option to foreclose or what has the Bureau looked at any other paths that we may be able to take going forward?

NICK HLUCHYJ: Well generally, say modifications or renewals, may also not require an ATR/QM analysis. I had the opportunity last week to speak with a multi-agency group of examiners and one thing we tried to do is coordinate with our fellow agencies to make sure we're all on the same page on a lot of these issues, and one of the questions that came through our Regs Inquiry Portals pointed out that if you consistently make modifications and renewals, while that may seem to benefit the consumer, the examiners may raise this as an issue with respect to compliance with safety and soundness.

And so I asked the examiners at this meeting last week, in what way might this be relevant? And the response from several of them, we had a lively discussion, is that, if the modification or renewal results in a viable loan, that's good, and that's good for the consumer and it's good for the institution. But if you keep doing modifications and renewals and stringing along a bad loan and keeping it on your books, then that may raise the question of whether additional capital requirements need to be in place. So again, you have to look at the whole big picture with respect to any particular loan, is this really turning it into a viable transaction or is something just being strung along to avoid a default and foreclosure?

ROD ALBA: Thank you Nick. Going onto the next slide, the issue of residual income.



ROD ALBA: For those members that lend outside of QM, or that land in the "rebuttable presumption" range of QMs, can the CFPB provide an overview of how lenders should determine residual income for purposes of the QM, I'm sorry, for purposes of the ATR rule?

NICK HLUCHYJ: The concept of residual income is, sort of goes hand-in-hand with the DTI. DTI tells you what proportion of debt the consumer may be carrying but the residual income gives a picture of how much income the consumer has after taking the debt into account to meet the daily living expenses of everyday life. And it comes personally relevant, it adds in additional facts to the consideration of DTI. You may have a high DTI individual who's also a high income individual and therefore, their residual income will be much more adequate to address his or her needs then the residual income of someone who may come in under 43% but is a low income individual and actually may have a more difficult time in meeting living expenses than is otherwise the case.

There's no explicit guidance other than taking into account known debt and the consideration of what the living expenses of the individual and that particular set of circumstances would be and in that area, the only agency that has addressed, with explicit guidance to the question of residual income, is VA and they actually prepared tables of what sort of adequate living expenses would be for particular income levels on a geographic basis because living expenses will vary from area to area.

To the extent that a lender's dealing in a particular area, this probably is going to be more familiar with what an adequate living expense is in that area, and will be taking that into account. To the extent that you're a national lender, it may be necessary to do some sort of reasonable analysis in which to place the residual income into context because, again, it's going to be context specific calculation.

ROD ALBA: Thank you Nick. So this is very important, we appreciate that. No explicit guidance, certainly rational, it has to be in good faith, reflective of the area or region where the loan is made or where the home is located and certainly we can be guided by VA and other programs. So that, but again, but explicit guidance for right now is going to be important for our members.

Going to the next slide, slide number 15.

ATR & QM Compliance

6. Treatment of Self Employed Individuals: With regard to DTI test under QM, could you provide some insight on how CFPB considers that the test should be applied to self-employed individuals?

   Specifically, with self-employed borrowers, many applicants show no profit, very little profit, or even losses on their taxes. Example: Applicant may show net income of $5,000 but have numerous deductions like depreciation and interest (generally added back for the business Debt Service Coverage ratio). Where the applicant is considering a residential purchase, the new ATR rules mandate that creditors calculate DTI. What income figure should the creditor use for DTI, assuming the self-employed borrower is not paying himself a salary?

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ROD ALBA: The treatment of self-employed individuals with regard to the DTI test under the debt-to-income test, under the QM, can you provide some insight on how CFPB considers that the test should be applied to self-employed individuals? This has certainly become a difficulty and has become very important for a lot of our smaller banks. We provide a bit of an example, with self-employed borrowers we state that many applicants show no profit, very little profits sometimes, or even losses on their taxes, the example we give is an applicant that may show a net income of $5,000 but has numerous deductions like depreciations and interest, generally added back for the business debt service coverage ratio.

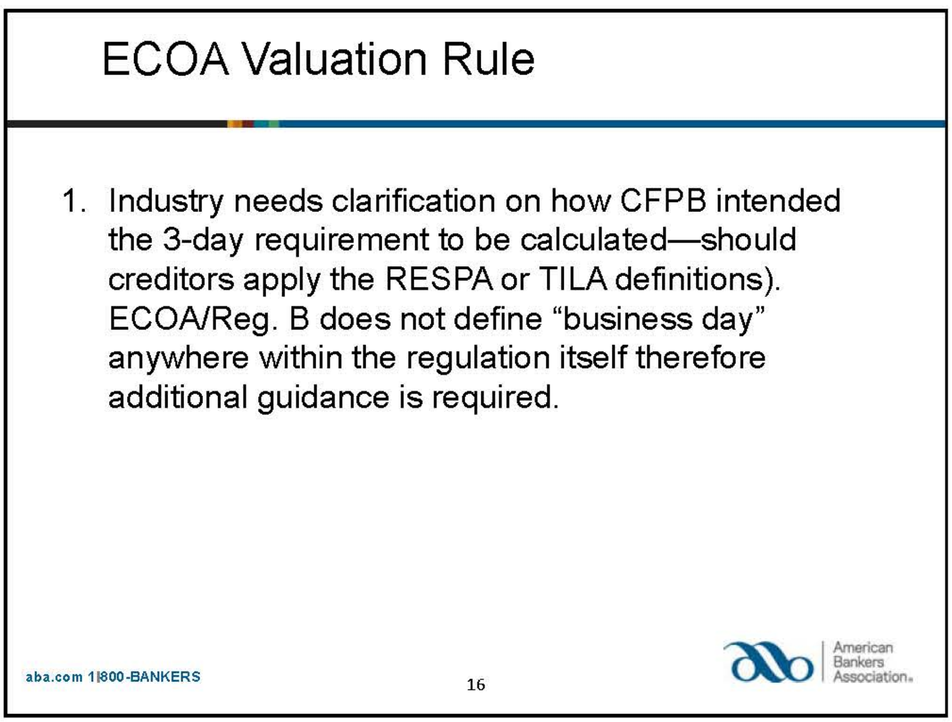
Where the applicant is considering a residential purchase, the new ATR rules mandate that creditors calculate the DTI. So, what income figure should the creditor use for DTI assuming the self-employed borrower is not paying himself a salary? Assuming that we are looking at the income from the business?

NICK HLUCHYJ: Pre[inaudible] and sole proprietorship are in, say, Chapter S corporation, the income and assets, the gains and losses of the entity are passed onto the individual. So, to some extent, there's an identity there of gains and losses, and that's basically the way that Appendix Q, which is used for computing DTI, for purposes for QM, is set up. There's a table that follows Section I(e) that states that depreciation or depletion may be added back into the adjusted gross income of the self-employed individual. And to that extent, there will be some increase in the gross income.

Paragraph F there deals with the small corporation which is basically a pass through entity. Paragraph G deals with Chapter S corporations. H deals with how partnerships are addressed. Basic rule is that in all these cases the depreciation or depletion can be added to adjusted gross income. Now the other consideration may be, with respect to self-employed individual is, do they have assets that can be relied on to demonstrate that they have the ability to repay. There is not a lot of guidance provided on the consideration of assets, although the commentary to the ability to repay section states that creditors can rely on practices of the GSEs in assessing assets and income, and for example, the GSEs have procedures for annuitizing assets. So that may be another avenue that can be considered in determining whether a self-employed individual actually qualifies under ATR/QM.

One question that the creditor may ask himself is how would such a loan be assessed prior to the ATR/QM rules, it could be that they may have relied heavily on the value of the property, that is being purchased or mortgaged, that has been taken out of the equation because in considering income assets, the property that is the subject of the transaction can't be considered. To the extent that lenders prior to ATR/QM assessed self-employed individuals, much of the same would follow, at the present time, with the exclusion of the property that's the subject of the transaction.

ROD ALBA: Thank you Nick. That gives us a lot to chew on. Going onto a question that is on slide 16.



ROD ALBA: Industry needs clarification on how the CFPB intended the three-day requirement be calculated for the ECOA evaluations rules. So we're moving from QM and into the ECOA evaluations rule. Should, when we look at this, certainly ECOA and Reg. B does not define "business day" anywhere within the regulation itself and so we're asking for more guidance. Should we perhaps apply the RESPA or the TILA definitions for three days? What would be the Bureau's preference?

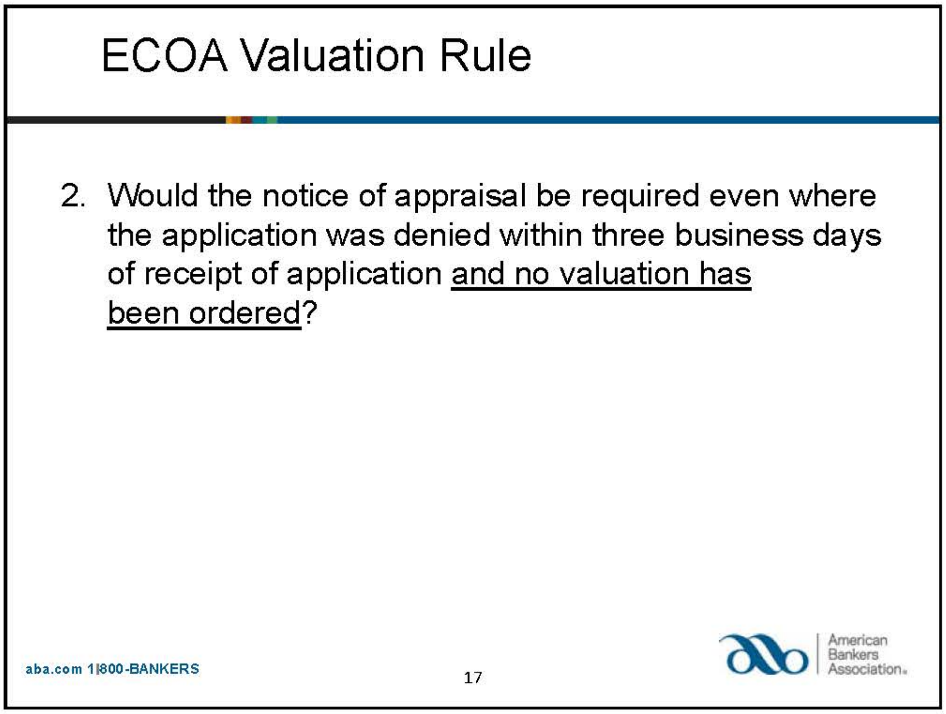
NICK HLUCHYJ: Well, for this question, there's no specific definition as you point out. In fact, that might be the only portion of Reg. B where "business days" is used, although, a touchstone on Reg. B itself may be at § 1002.11, which deals with how state laws are applied and whether or not they are preemptive. And the general statement there is that Reg. B preempts only the laws that are inconsistent with the Act. So for example if "business day" is defined under state law, that doesn't seem to be something that would be preempted under ECOA and the state definition could be relied upon.

It's a difficult question even with the established definitions, which often refer to the days when your offices are open for transactions. If you're dealing mainly out of a website, that's open seven days a week, does that constitute a "business day" for you? And this is an area in which regulation has to catch up to practice, I think. But with respect to this specific question, I believe that the state definition, if there is one, of "business day," can be relied upon.

ROD ALBA: Okay so, "can be relied upon," I, I, on this one, let me just push this just a little bit more. If someone decides to adopt only RESPA just to make it all of their practices, I guess, just to make it a uniform definition to ease compliance, would that be acceptable or are you saying that we must look at the state?

NICK HLUCHYJ: Well, if the RESPA definition is not consistent with state law, I believe that the law would trump your adoption of something else.

ROD ALBA: Okay, thank you. That is clear enough. Let me go on to the next, it may be a little bit scary but it's clear enough, we may be in communications again. On item number 17, on slide number 17, we reached the first, the end I guess of the first phase.



ROD ALBA: Again, dealing with the ECOA valuations rule, Nick, would the ECOA disclosure valuation materials, the ECOA's, I'm sorry, the disclosure of valuation materials be required even where the application, the consumers, the customer's application was denied within three days of receipt of application, and this is what's important, and no valuation had been ordered at that point?

NICK HLUCHYJ: This is a question that the regulation, at 1214(a)(2), that is in question here, only states that, a creditor shall mail or deliver to applicants not later than the third business day. And so that's the relevant language. There do not appear to be any exceptions to this requirement and, for example, to maintain a level playing field between a creditor who adopts sending the notice out on the first day, after receiving an application as opposed to someone who is waiting until the last minute to see whether the application would even be considered.

There's nothing explicit in the regulation that would exclude sending the notification out even if it's obvious that the transaction will not be consummated within the first three days.

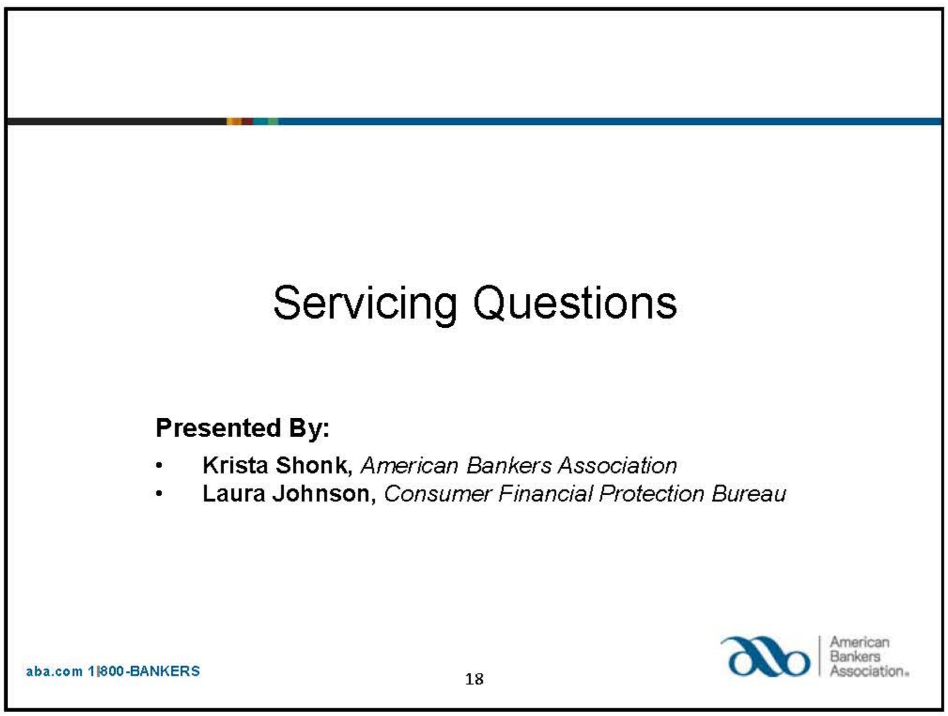
As a practical question, and this is something that perhaps you could shed some light on. I don't mean to turn the tables on you but is this a relatively common situation? Where, or is this the sort of the exception rather than the rule that is going to occur that often?

ROD ALBA: Yeah I would guess that it is somewhat of an exception but it occurs with sufficient frequency that it was voted as one of the top questions that the bankers had. So I would say that this is going to be an issue for generally for the industry going forward.

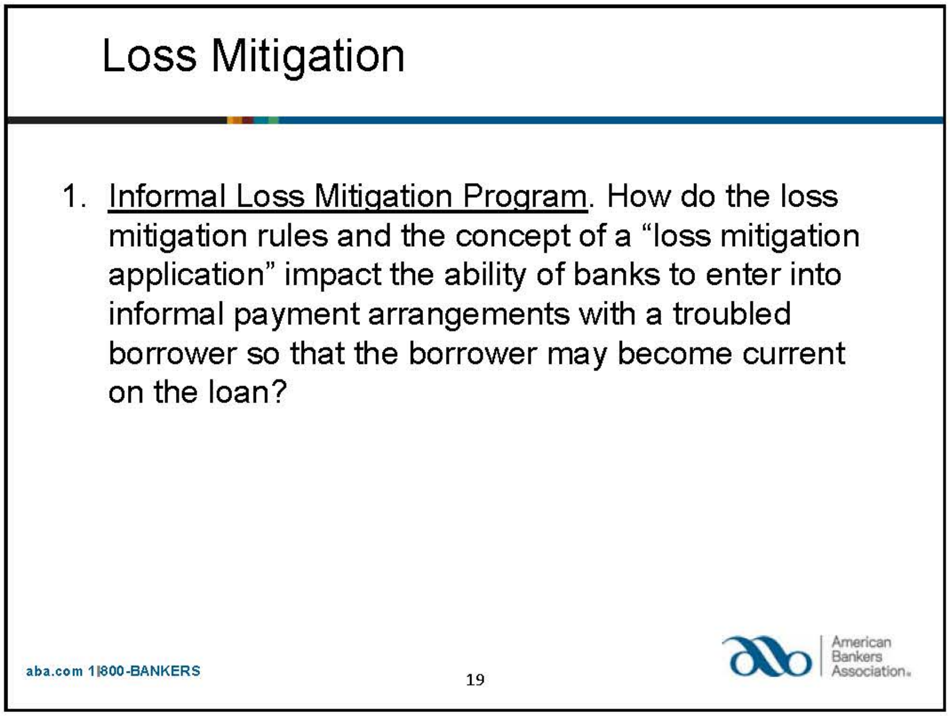
NICK HLUCHYJ: Okay, as I said, there didn't, there is nothing upon which to base an exception on in these circumstances.

ROD ALBA: Okay, we may be communicating with you on this item. I think that maybe perhaps we could play with just the definition to the extent that a valuation, to the extent that there is any internal process to just assign a value, to the extent that we don't have to go out and explicitly get a valuation or an appraisal that would be given free to a consumer that eventually is not interested in the loan. May be a good accommodation in the sense that we may just be able to do some sort of, lesser form of appraisal or valuation method and again, be able to provide the consumer with something. We may be able to reach, we may be able to give some recommendations to the Bureau that would achieve some accommodation here, so, we certainly will be back to you when we consult this item with our membership.

With that, let me pass it on to Krista as we move onto the servicing questions.



KRISTA SHONK: Thanks Rod.



KRISTA SHONK: You know, it wasn't that long ago that our members were just laser-focused on managing their vendors, and were working on completing the necessary interfaces and programming required to comply with the Bureau's periodic statement rules. But I think just about everyone was able to get over that hurdle, or most of that hurdle, and now ABA has started to receive a lot of inquiries related to the loss mitigation rules. So that's where we'll begin the servicing portion of today's program.

Laura, the vast majority of our members are community banks, and they have a strong history and a strong culture of working with their borrowers who may have fallen on some hard times. And in most cases, this type of, I guess what I would call, high touch servicing, has resulted in informal payment arrangements with the borrower. But these banks still have some lingering uncertainty in terms of how they should apply or should adjust these practices to the CFPB's loss mitigation rules.

So I was wondering, from a jumping off point, if you could just educate us on how the new loss mitigation rules and this concept of a loss mitigation application impact the ability of institutions to enter into informal payment arrangements with a troubled borrower so then that borrower can get back on their feet and can become current again?

LAURA JOHNSON: Sure. Thanks, Krista, and thanks for inviting us to come and be here today. With respect to your first question, we certainly understand that several smaller community banks have entered into these types of formal and informal payment arrangements with troubled borrowers in the past to work with them to try to come current.

If the bank meets the definition of a small servicer, then the bank is not subject to the loss mitigation processes for taking and evaluating applications. So those small banks would still be able to continue entering into informal payment arrangements such as these, without really needing to change anything to meet the loss mit application processes and the rules, because those processes do not apply to small servicers.

If the bank is not a small servicer, it is subject to all of the loss mitigation rules, including the loss mitigation application process requirements. So you would need to look at whether any of these informal payment arrangements would meet the definition of a loss mitigation option, under the rules.

Our definition of loss mitigation option is pretty broad. It's defined as an alternative to foreclosure, offered by the owner or assignee of the mortgage loan, that is made available through the servicer to the borrower. So these informal arrangements may very well meet that definition.

As a result of that, the impact of the rules on the banks informal payment arrangements, would depend on what that arrangement is. Maybe the easiest way to kind of explain this is to take an example. So let's say the borrower's monthly payment is $900 and the borrower had a large car repair, a large car repair bill that month and misses a payment. She comes into the servicer and suggests that she could possibly pay an extra $300 a month, over the next three months to make up the missed payment. If the borrower comes in and asks for help and provides this type of information, that looks a lot like an incomplete loss mitigation application. And the rules have a general prohibition that servicers cannot offer a loss mitigation option based on evaluating an incomplete loss mitigation application.

However, there is an exception: servicers can offer a short term payment forbearance program to a borrower based on the evaluation of an incomplete application. As a reminder, under our rules, a short term payment forbearance program is where the servicer allows the borrower to forego making certain payments, or portions of payments, that are due over periods of no more than six months.

The program would be considered short term regardless of the amount of time the servicer allows the borrower to make up missing those, to make up those missing payments.

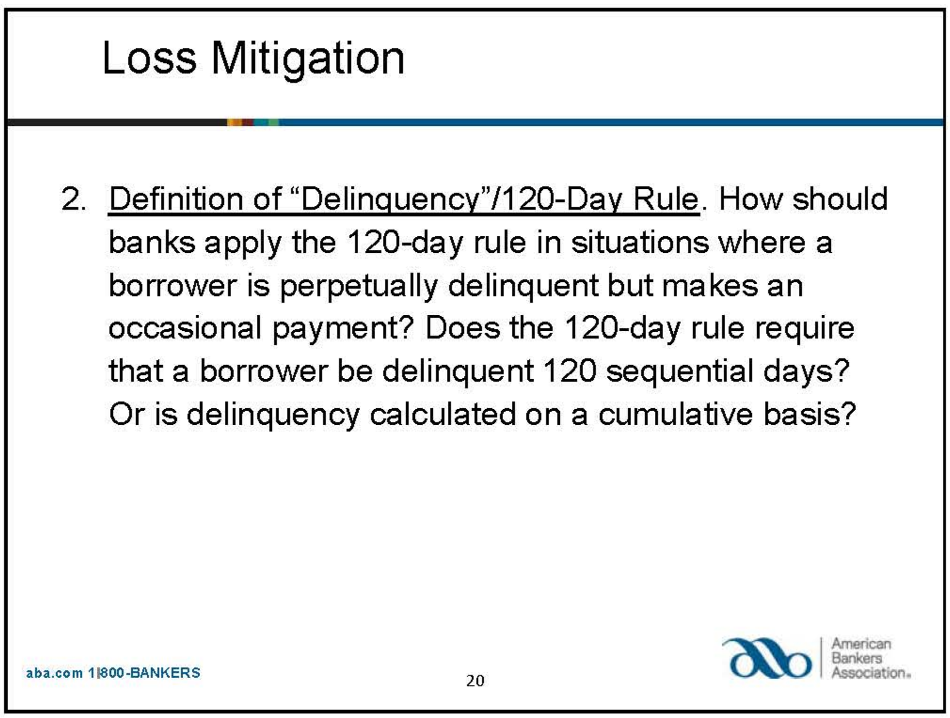
So, based on an evaluation of an incomplete application, the servicer could offer the short term forbearance program where the borrower would pay an extra $300 per month over three months. In that circumstance however, the servicer still should provide the borrower with a note that lets the borrower know that she may complete the application to receive a full evaluation of all of the loss mitigation options available to her.

But permitting this type of short term forbearance under the rules without having to evaluate a complete application allows the borrower's short term problems to be addressed while still preserving the borrower's single use of the full loss mitigation protections in § 1024.41.

Then the next question is, well what if the borrower asks for something that is not considered a short term forbearance, that would be some other type of informal loss mitigation option.

Again, this would be considered an incomplete loss mitigation application under the rules. And the servicer would need to go through all the regular loss mitigation application processes. So that would include sending the acknowledgement notice that states the application is incomplete, exercising reasonable diligence in obtaining documents and information to complete the application, and then finally if the borrower does complete the application the servicer would evaluate that borrower for all options available to the borrower and offer a loss mitigation option if applicable.

KRISTA SHONK: Thanks for that, just kind of, baseline, just kind of doing a quick level set for all of us. Another topic that our members have raised frequently in the last few weeks involves various issues related to the 120 day, the 120-day rule, which I'm sure as everyone will recall, this rule prohibits servicers from issuing the first notice or filing for foreclosure until the borrower is more than 120 days past due.



KRISTA SHONK: Laura, can you talk about a couple of things? With respect to, what does it mean to be delinquent for purposes of the 120-day rule, and I guess, a related

question to that is how should banks calculate delinquency for purposes of the 120-day rule? And, in particular, is that a sequential basis or is it done on a cumulative basis?

LAURA JOHNSON: So you're not going to like the answer to this question. As you know, there is no definition of delinquency for purposes of Regulation X § 1024.41 and the 120-day rule. As you know, there are definitions for the early intervention and the continuity of contract requirements under Reg. X but those definitions are limited to those, to those specific sections. There's also no provision in Regulation X that really discusses how to define undefined terms. So, in light of the lack of definition, the guidance that we've been giving is that servicers should look to common principles of undefined terms. That would include looking to state law or contracts law and industry standards.

One thing to keep in mind is, you know, servicer should consider the amount of risk that they're comfortable with in this area and also remember that there's a private right of action under § 1024.41. This is something that we have certainly been getting questions about, I know you all have gotten a lot of questions and I just want to reassure everyone that we are continuing to monitor this issue.

KRISTA SHONK: Okay. Well I guess we'll have to sit tight, then, on that one. A related issue involves situations where a borrower may be behind on his or her mortgage and the bank then sends a letter recapping the past due amount and saying that the bank will begin foreclosure if the borrower doesn't pay the full amount past due, in about 30, or in 30 days. So, how should banks handle situations where they've sent the letter, the delinquent borrower makes one month payment as opposed to paying the full amount past due? And, so when this happens, is the bank required to accept a partial payment and in this, this scenario, when I says partial payment, that is just one month payment, as opposed to the full amount past due? Or can a bank require the borrower to bring the full amount past due in order to bring the loan current? And this is really designed, this is really getting those situations where you have what I would call a serially delinquent borrower, where this cycle kind of just repeats itself time after time?

Loss Mitigation

3. Delinquency and Partial Payments. Banks commonly send to delinquent borrowers demand letters that recap the past due amount and state that the bank will begin foreclosure proceedings if the borrower does not pay the full amount past due within 30 days. How should banks handle situations where a delinquent borrower makes one month's payment instead of paying the full amount past due? Must a bank accept partial payment (e.g., one month's payment) or may it require the borrower to pay the full amount past due to bring the loan current?

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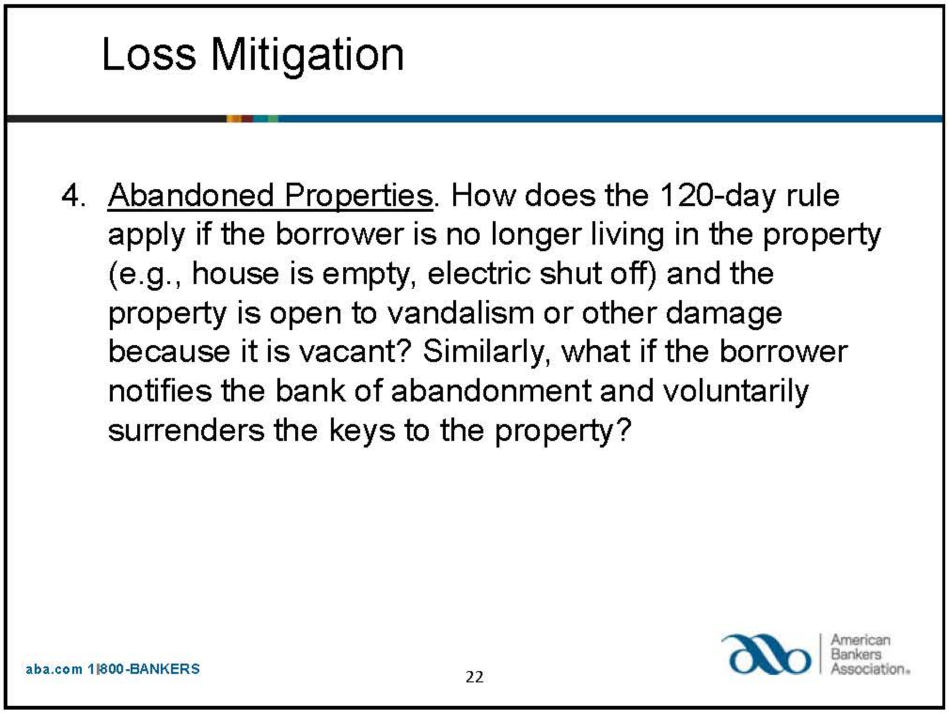
LAURA JOHNSON: Right, so it sounds like this question is getting at, sort of, how to apply payments after acceleration.

KRISTA SHONK: Right.

LAURA JOHNSON: First, it's important to note that our rule does not prohibit acceleration. At acceleration, the new periodic payment would be the total amount due. So the servicer can ask for the full amount. To your specific question about a partial payment, the servicer does have the option of accepting a partial payment and applying it or putting it in suspense as always.

As a reminder, if the servicer does retain the partial payment in suspense, then the servicer should disclose that total amount of the funds held in suspense on the consumer's periodic statement, if a periodic statement is required.

KRISTA SHONK: Shifting gears a bit, but moving on to the next slide and still staying with the 120-day rule, let's talk a little bit about abandoned properties, which is another very commonly discussed topic within our membership.



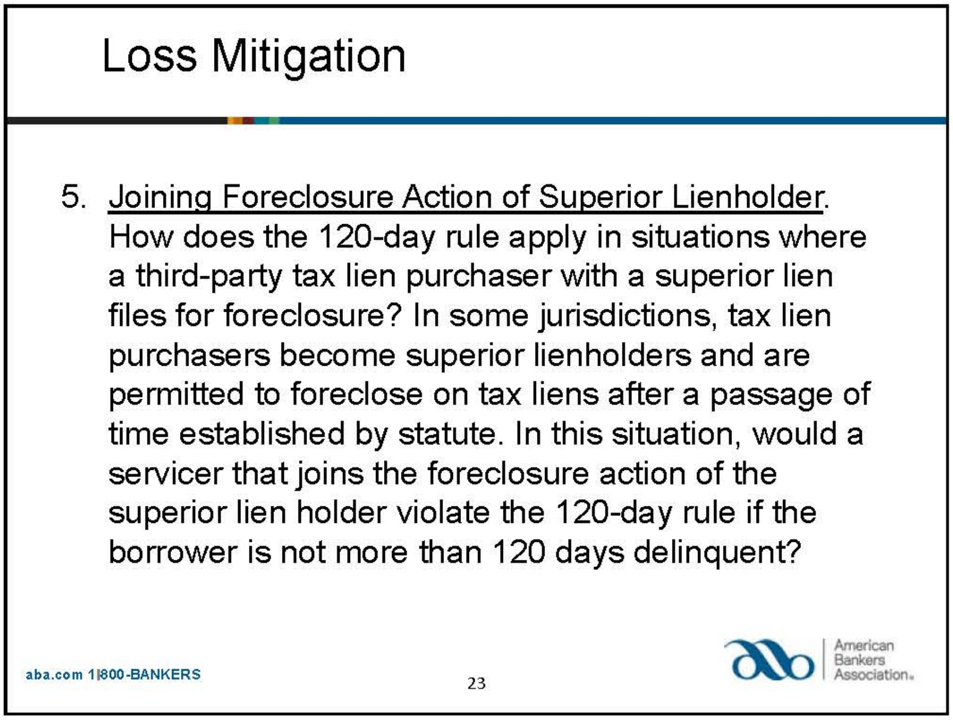
KRISTA SHONK: What can a bank do to protect its interest if a borrower is delinquent, the borrowers no longer living in the property, the house may be empty, the electric is turned off, and then the property is open to vandalism or other damage because it's, it's vacant? I guess a first cousin to this question, what if the borrower notifies the bank of abandonment, turns over the keys, what can a bank do to preserve its interest in light of the 120-day rule?

LAURA JOHNSON: Sure. We have received numerous questions about making determinations on when a property is vacant or abandoned. The key here is that the loss mitigation rules, including the 120-day rule, apply to a mortgage loan that is secured by a property that is the borrower's principal residence. And just as a point of reference, the scope provision that servicers should look to, for purposes of this section, are the scope, is in § 1024.30 of Regulation X and that defines the scope of applicability of the mortgage servicing regulations that are in subpart C. It's slightly removed from that exact provision, so it's kind of helpful to point that out sometimes.

So we've said before, and, and, we'll say again here, a vacant property may still be a principal residence. So for example, someone who may be serving overseas may not be physically in the property and the property could, you know, appear to be vacant. The house is empty, the electricity may be shut off. Nonetheless, that still could be the consumer's principal residence.

On the other hand, an abandoned property, may not be a principal residence. There's, the difference between vacant and abandoned can be a very fact-specific determination and frankly, our servicing regulations do not provide additional guidance in this area. Servicers have to make the determination. One overall suggestion is that servicers should be sure to explain in their policies and procedures how they are making the determination of whether the property is a principal residence.

KRISTA SHONK: Okay. Moving onto the next slide.



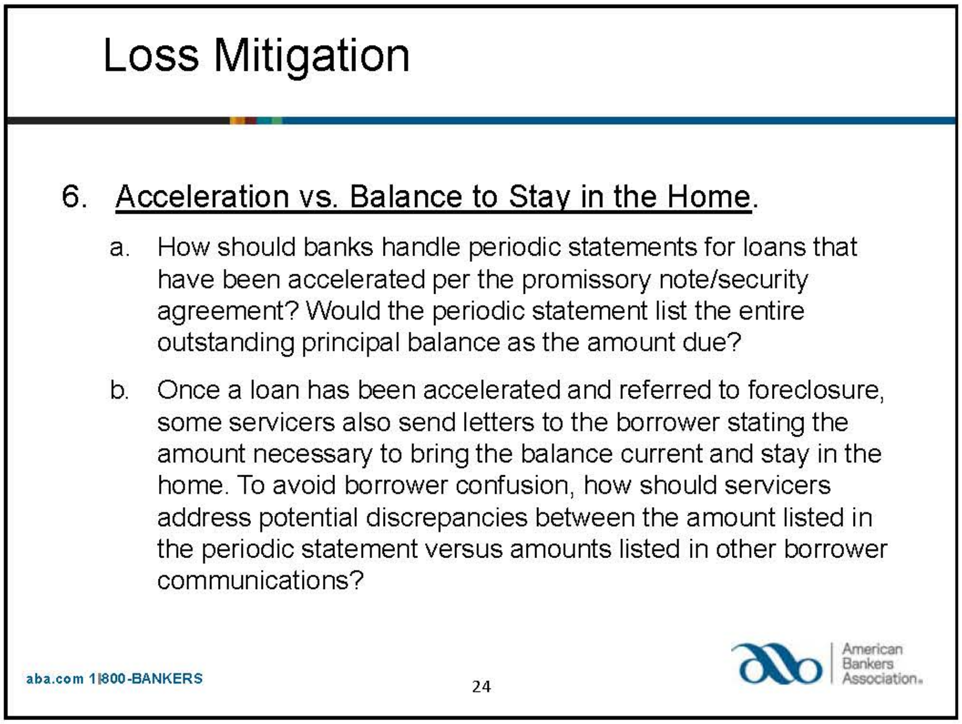
KRISTA SHONK: Again, still staying with the theme of the 120-day rule, this is the last one, I promise. Laura, can you talk about how the 120-day rules, or the rule, applies when a superior lien holder files for foreclosure? I think the rule's pretty clear on the case of the junior lien holder, but our banks are kind of tripping over the senior lien holder scenario, and in particular just to give everyone a little bit of background on this, this issue has come up in jurisdictions where a borrower hasn't paid his or her property taxes and the locality sells that tax lien to a third party and there is quite an, I wouldn't even it call it a cottage industry, it's bigger than a cottage industry out there on third party tax liens, and that, that tax lien purchaser then becomes this superior lien holder, and they're, they are permitted to foreclose on the tax lien after a passage of time set by statute.

So, in this situation, would a servicer that joins the foreclosure action of a superior lien holder, violate the 120-day rule if the borrower is not more than 120 days delinquent? And interestingly enough, our members are telling us that it's not uncommon for a bank, to be a bank, a borrower, to be current on their mortgage but not pay their property taxes.

LAURA JOHNSON:** Yes, and this a question that we've heard several times as well. Again, just as a reminder, § 1024.41(f)(1) prohibits servicers from making the first notice or filing in a judicial or non-judicial foreclosure process until a borrower is more than 120 days delinquent. As you noted, there is a carve-out that a servicer may join the foreclosure action of a subordinate lien holder, but there is no corresponding carve-out to allow servicer to join a foreclosure action of a lien holder or a superior lien holder.

However, if it's allowed under the contract, or state law, the servicer may accelerate the note and if the borrower does not pay the full amount, then the servicer can start the foreclosure process 120 days later.

KRISTA SHONK: Okay moving onto the next slide.



KRISTA SHONK: Some of our members have submitted questions seeking guidance on how to communicate with borrowers whose loans have been accelerated. This is a multiple part question, so let's just take them one at a time and walk through it.

First of all, just to make sure we're all starting from the same level of information, how should banks handle periodic statements for loans that have been accelerated? What would the periodic statement list as the amount due?

LAURA JOHNSON: So as an, so as an over, an overall comment, as you know, the periodic statement is designed to improve, to provide important and non-confusing information to borrowers, including the amounts that they're expected to pay. It also should reflect the legal obligation between the parties.

We understand that there could be some borrower confusion after acceleration, particularly, where the contracts may permit servicers to accept a reinstatement amount that would be less than the entire outstanding principal balance.

As a general reminder, servicers can add information to the periodic statement, as long as it doesn't overwhelm or obscure the required disclosures or violate specific grouping requirements. So the periodic statements can reflect the entire outstanding balance as the amount due, or it could actually reflect the reinstatement amount as the amount due. But the important piece is that either way the statement should include both amounts and explain what they mean so as not to confuse borrowers. Remember that the periodic statement has a clear and conspicuous disclosure standard. So disclosures must be in a reasonably understandable form. I think that probably leads into the second question.

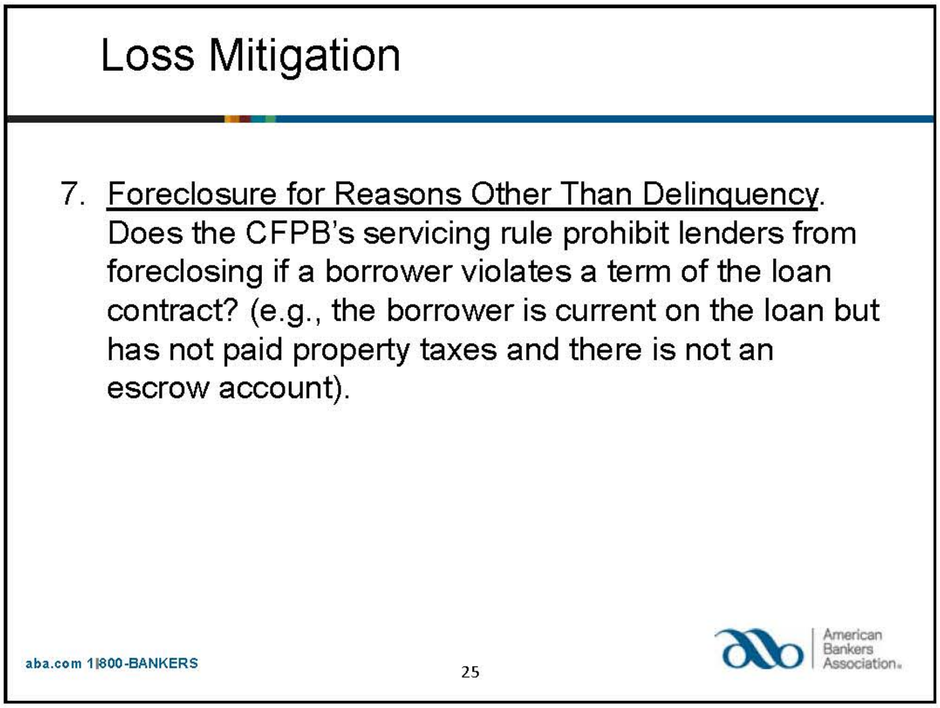
KRISTA SHONK: It does and I think maybe, you, maybe partially--

LAURA JOHNSON: Partially.

KRISTA SHONK: Partially answered the second question, but let's just kind of recap to make sure that we're all just kind of, in alignment here. So, I think our members submitted these questions with the concern that if they reflected the full amount due on the periodic statement, that is the entire loan balance, or principal balance, but yet still sent letters and other forms of communication to the borrowers suggesting that if they paid a lessor amount to bring the loan current, and reinstate the loan, that that would potentially be confusing to borrowers and they didn't, they didn't want to create that type of situation but at the same time, they wanted to offer the borrower another out and avoid foreclosure if at all possible. So I think what I hear you saying, is that could be addressed by tweaking the periodic statement a bit to include the full amount of the unpaid principal balance along with a potential note regarding the amount to reinstate as long as the clear and conspicuous standard were complied with.

LAURA JOHNSON: Right. That's exactly right. Again, the sort of overriding principle here to remember is that the periodic statement is supposed to provide important information to borrowers and non-confusing information to borrowers.

KRISTA SHONK: Yes. Okay, that's helpful. Thanks. Moving onto the next slide.



KRISTA SHONK: Foreclosures for reasons other than delinquency. We have gotten this question a lot. So I'm anxious to hear your views on this one. Does the CFPB's rules prohibit lenders from foreclosing if a borrower violates a term of the loan contract that's unrelated to the payment, the monthly payment of the loan? So, and the classic example that has really started to bubble up, I'd say the first quarter of this year involves property taxes. So if, what happens if the borrower is current on the loan and hasn't paid property taxes, of course that assumes no escrow account? What then? And, there are a million variations on this, but I think that kind of gives us a good example that we can all probably work from.

LAURA JOHNSON: Right, and again, I feel like I'm repeating myself a little bit with reminding everybody again that the loss mitigation section prohibits the servicer from again, making the first notice or filing unless the borrower is more than 120 days delinquent on the mortgage loan obligation, and that's a key phrase. There are a couple of other options for making the first notice or filing, one is if the foreclosure is based on a violation of a due-on-sale clause, and the other one, which we mentioned before, is if the servicer is joining a foreclosure action of a subordinate lien holder.

But specific to this question, if the borrower is violating the term of the loan contract other than a due-on-sale clause, and there is no subordinate lien holder situation, then you do have to go back to the 120 days requirement. So again, it's, the servicer cannot make the first notice or filing unless the borrower's mortgage loan obligation is more than 120 days delinquent. So the—

KRISTA SHONK: Okay. Sorry, sorry go ahead.

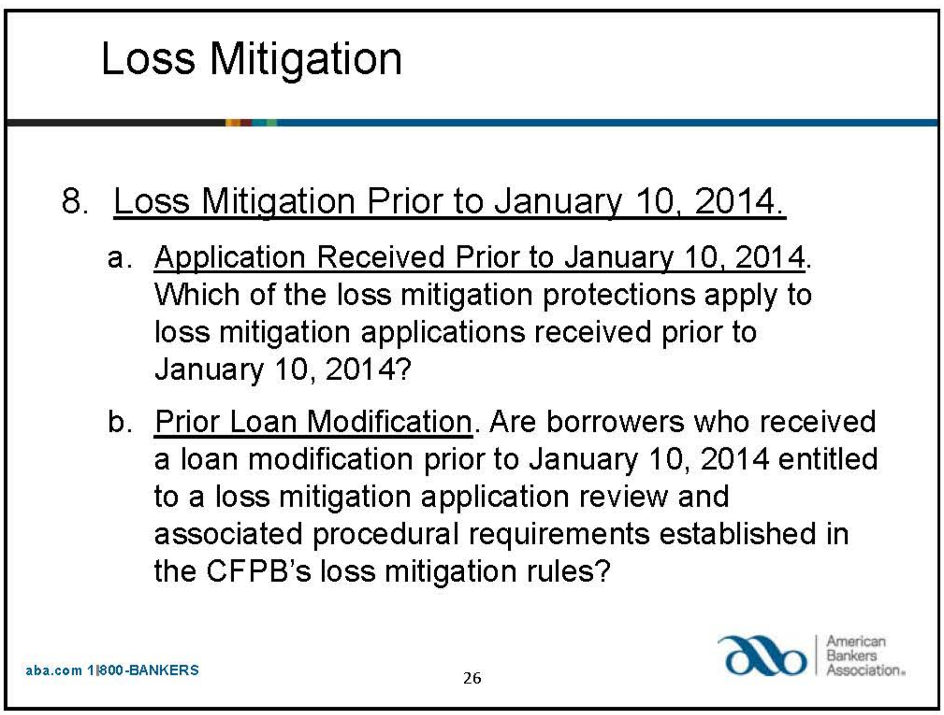
LAURA JOHNSON: I was going to say, so there's some admittedly kind of gray area around what exactly the mortgage loan obligation is, and we've generally been interpreting that to refer to principal, interest, and escrow, as applicable.

So it would not include unpaid non-escrow taxes if the borrower is otherwise current. One thing to remember here is that there is a private right of action under this section. So if a servicer considers interpreting mortgage loan obligation more narrowly, for example, if they wanted to make the first notice or filing when the borrower is 120 days delinquent on non-escrowed taxes, that servicer could find frankly, could find itself being sued by a borrower.

A court could take a more conservative view of mortgage loan obligation. So again, here is a situation where it really is up to the institution to determine that interpretation and the legal risk that they're the most comfortable with.

One additional note, and this is again, repeating things that I've said before, but if the servicer has a borrower that is not paying non-escrowed taxes or another similar scenario, if it's allowed by the contract, the servicer could accelerate the loan and then the full outstanding balance would be due. So if the borrower does not pay that full outstanding balance in 120 days, then the borrower would be considered more than 120 days delinquent on the obligation and the servicer could begin the foreclosure process.

KRISTA SHONK: Okay, so we're finally to the last question on loss mitigation.



KRISTA SHONK: And let's just talk a little bit about the applicability of the loss mitigation rules. I know there's been a little bit of confusion within our membership regarding when a, what they are required to do when a loss mitigation is received in various points in time.

So just to, looking at points A and B, we'll just, we'll just walk through those. What happens if a bank receives a loss mitigation application? What if they received it before January 10th? So what if January 1st, they got a loss mitigation application and so there, hopefully by now they've worked through that process, but then the borrower for whatever reason comes back to them tomorrow? What is that bank required to do?

LAURA JOHNSON: Sure. So, the effective date was January 10th and servicers are not required to comply with, or were not required to comply with the loss mitigation rules, with respect to loss mitigation applications that were received prior to that date.

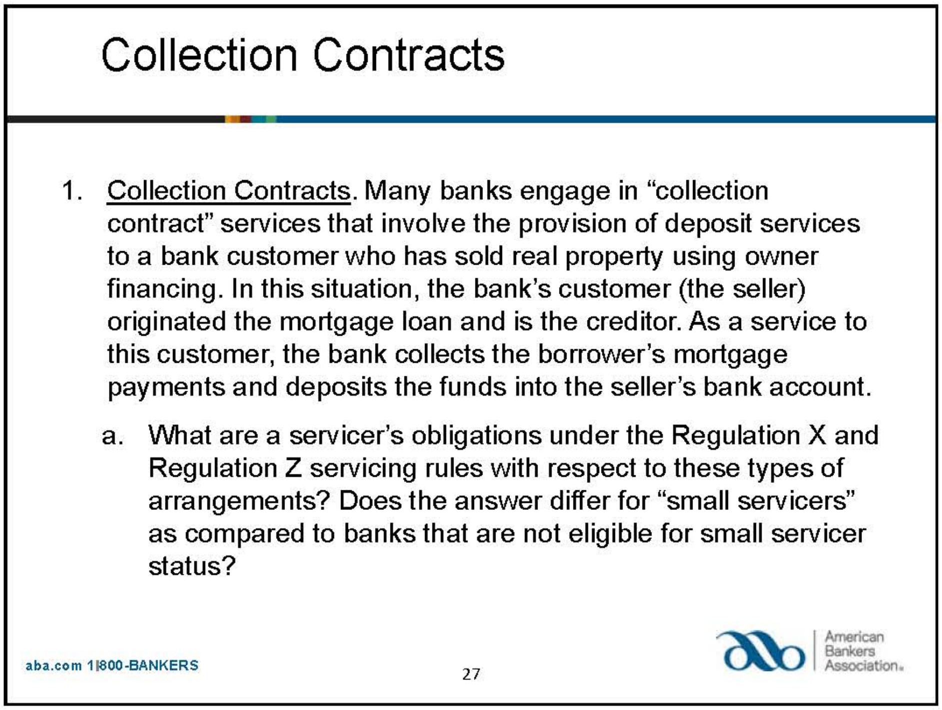
KRISTA SHONK: And so, that means that even though there was an application, say January 1st and the borrower comes back tomorrow, they would be required to go through that process again?

LAURA JOHNSON: Right. Right. So borrowers do have the right to be evaluated for loss mitigation options for applications that were received on or after January 10th. This is true even if the borrower was previously evaluated for loss mitigation or even had already received a loan modification prior to January 10th. I will note that the 120 day prohibition on foreclosure referral applies both to loans that became delinquent on or after January 10th and also to loans that were already delinquent on that date, but for which the servicer had not yet made the first notice or filling for foreclosure.

KRISTA SHONK: Okay, so even if a borrower got a mod, say as part of the big, the big camp push a couple of years ago-- say 2010, they got a mod. They still just, you know, they had another life event and things are not working out for them, they could submit another loss mitigation application today, and they would be required to be evaluated under the current rules. Is that right?

LAURA JOHNSON: That's correct.

KRISTA SHONK: Okay. Well that wraps up our questions on loss mitigation.



KRISTA SHONK: We'll just advance to the next slide. Let's talk a little bit about something called, at least what some bankers call "collection contracts." They are known by land contracts and a variety of other names as well, but I think the same general set of facts, or, or practices apply. So, for those of you who may not be familiar with collection contracts, many banks particularly smaller banks, engage in these services that involves providing deposit servicers, excuse me, providing deposit services to bank customers who have sold a piece of real property, have owned or financed that property, but they don't want to be responsible for collecting payment from the purchaser of that property. So, in this situation, the bank's customer, that is the seller of the property, actually originated the loan, they're the creditor of the loan, and the bank is just then collecting the mortgage payments and depositing them into the seller's bank account.

And there are a few variations on this, but that's just kind of the general fact pattern. And some banks have, you know, a few of these, some of them may have a couple of dozen of these, and so we've been getting some questions in terms of how this type of arrangement impacts a bank's obligations under the servicing rules? And a couple of scenarios have come up. And the questions can kind of be put into two buckets: first of all, what are a servicer's obligations under Reg. X and Reg. Z with respect to these types of arrangements? And then, a second question we've been getting, which is very much related to the first, but, how do the rules apply, perhaps differently, for small servicers that may be engaged in this practice?

LAURA JOHNSON: Sure. So, this question is a little complicated actually. We've heard different terminology, again, used to refer to different types of arrangements that may kind of fall under the same question.

Essentially, you, well first of all, you need to look at the details of the loan itself to determine whether it's a federally related mortgage loan, and if it is, then you're subject to RESPA and Regulation X and the provisions there that apply to federally related mortgage loans.

If it's a closed-end consumer credit transaction secured by a dwelling, then you would be subject to TILA and Regulation Z and the provisions that are applicable to those types of transactions. For the most part, because these loans are seller-financed, they are likely to not be considered federally related mortgage loans for RESPA purposes. But again, I can't speak to every single factual situation that may come up so I don't want to say that 100% across the board. But moving sort of to the next point, in general, the term servicer and servicing are pretty broadly defined. So in this situation, it is possible the bank could be a servicer under TILA and would need to comply with the applicable requirements under TILA and the Regulation, in Regulation Z, unless the bank meets the small servicer exemption.

So, as a reminder, to be a small servicer, you must service together with any affiliates, 5,000 or fewer mortgage loans, all of which you must have owned, own or have originated. So, so the way that this type of contract comes into play here is that servicing even one of these seller-financed loans could potentially knock a servicer out of the small servicer exemption because the loan was not owned or originated by that servicer or an affiliate.

I will mention that there is a carve out for certain loans, that the servicer does not have to consider when counting the 5,000 loans for determining whether it qualifies as a small servicer. The servicer does not have to count a loan that it voluntarily services for a non-affiliate as long as the servicer does not receive any compensation or fees. So if a servicer is voluntarily servicing one of these seller-financed loans, then it would not have to include that loan in its small servicer determination. And that loan if it otherwise would be a small servicer would not knock that servicer out of that eligibility.

As I mentioned before, if a servicer does not qualify for the small servicer exemption, then to the extent that the seller-financed loans are not federally related mortgage loans, the servicer would not have to comply with the servicing requirements under Regulation X for that, for those loans but that servicer would still be required to comply with the servicing rules under Regulation X with respect to any other federally related mortgage loans that are on its books. And then again, finally, the servicer would have to comply with the applicable requirements under Regulation Z with respect to the seller-financed loans if they are considered closed-end consumer credit transactions secured by a dwelling.

Again, the Bureau is, has received numerous questions on this area and it's complicated, obviously. We're continuing to monitor this issue.

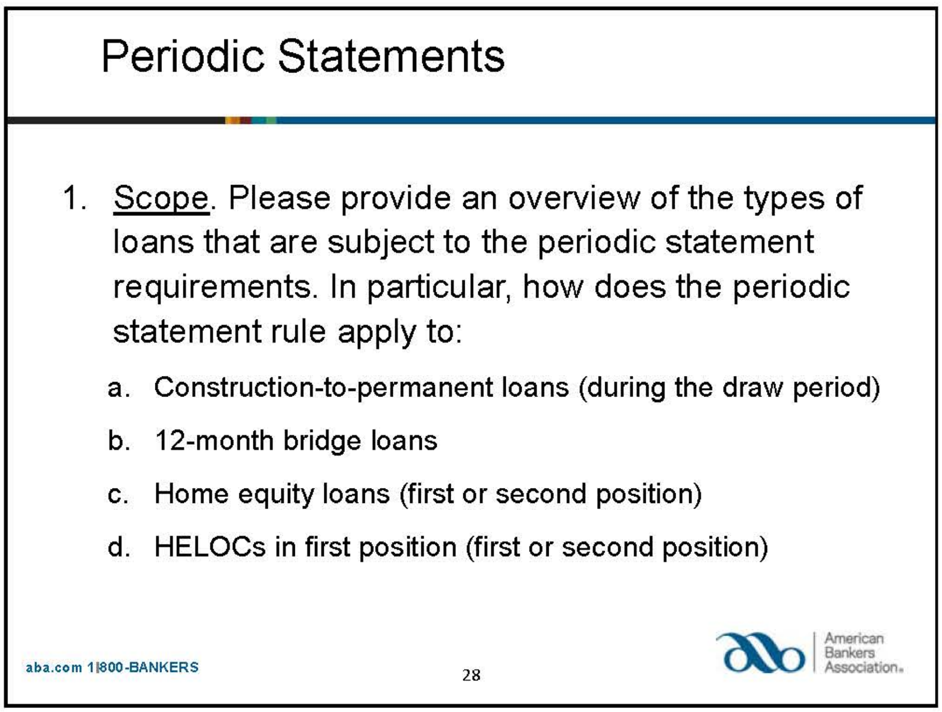
KRISTA SHONK: Okay. Before we, before we leave this, I just want to go back to a point you made earlier with respect to small servicers. And I know one question that came up fairly often, I guess, toward the end of the year, involved that exception for, I think, the Bureau refers to in the preamble as charitably serviced loans--

LAURA JOHNSON: Right, yeah.

KRISTA SHONK: And can you confirm that, that's for, that applies to all types of, you know, mortgage loans as long as a borrower doesn't receive a fee? It's not limited to non-loans to nonprofit entities.

LAURA JOHNSON: Correct.

KRISTA SHONK: Okay so that's the, we'll wrap up the collection contracts and move onto some of the questions involving periodic statements.



KRISTA SHONK: And I'll just preface this section of the program by saying that some of these questions are not going to strike many of you as particularly new or newsy, but they are questions that we have continued to receive over time and that we continue to receive in our e-mail box as we solicited, solicited inquiries for today's program. So I think with that in mind, it would be helpful just to, just to do a recap on some of these issues regarding periodic statement.

First, let's just talk about scope. Can you just give us an overview of the types of loans that are subject to the periodic statement requirement? This one continues to percolate, even as of last week.

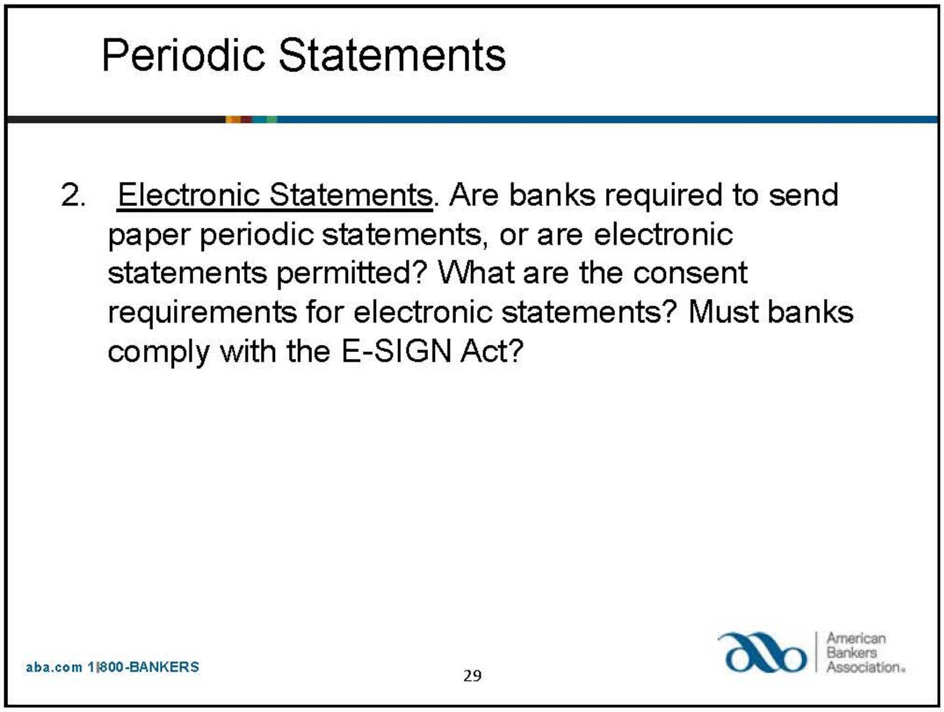
LAURA JOHNSON: Sure. So, the periodic statement requirement applies to closed-end consumer credit transactions secured by a dwelling, unless a specific exemption applies. There's some exemptions in § 1026.41(e). Those exemptions include things like reverse mortgages and time share plans. Notably, with respect to the, sort of the list of the types of loans that are mentioned here, there are not exemptions in that section for perm construction, construction to perm loans, or 12 month bridge loans, or closed-end home equity loans in a first or second lien position. So, to say it another way, yes, the periodic statement rule does apply to those types of loans, the first three I believe that are listed. However, the periodic statement does not apply to an open-end home equity line of credit. And we understand that there has been some concern coming up about whether the periodic statement requirements apply to HELOCs when there's a draw period that's followed by a set repayment period.

The periodic statement rule is not an attempt to change what is considered an open- or closed-end loan. So a repayment phase that's contemplated in the original HELOC agreement where the credit is replenishing, that is not considered a conversion to a closed-end transaction.

The current regulations and interpretations in this area remain unchanged. There's language, there's specific language in Regulation Z comment 40 paragraph 5 that provides some relevant guidance to determine whether the closed-end or the open-end provisions apply in this area to specific types of product.

If a HELOC is actually modified to create a closed-end transaction, or if it's rescinded and replaced by a closed-end transaction, then it would be subject to the requirements for closed-end periodic statements. So hopefully that helps clear that area up.

KRISTA SHONK: I think, I think that's helpful background for everyone to have. Moving onto the next slide, with respect to electronic statements.



KRISTA SHONK: A lot of times when we talk to our members, they express concern and rightfully so, about just their very significant increase in cost with respect to mailing periodic statements. So it may be helpful just to review whether banks are required to send paper statements? Is there an electronic statement option they can take advantage of, and if they can send electronic statements, what types of consumer consent do they need to get for that? Do E-Sign standards apply?

LAURA JOHNSON: Sure. So, the Truth In Lending Act, §128(f)(2) specifically provides that periodic statements may be trans-, may be transmitted in writing or electronically. Under the implementing regulations, a servicer is not required to provide electronic statements, but it is not prohibited from doing so either. So the servicer may provide electronic statements if the consumer affirmatively consents to receive them and that consent must be in advance.

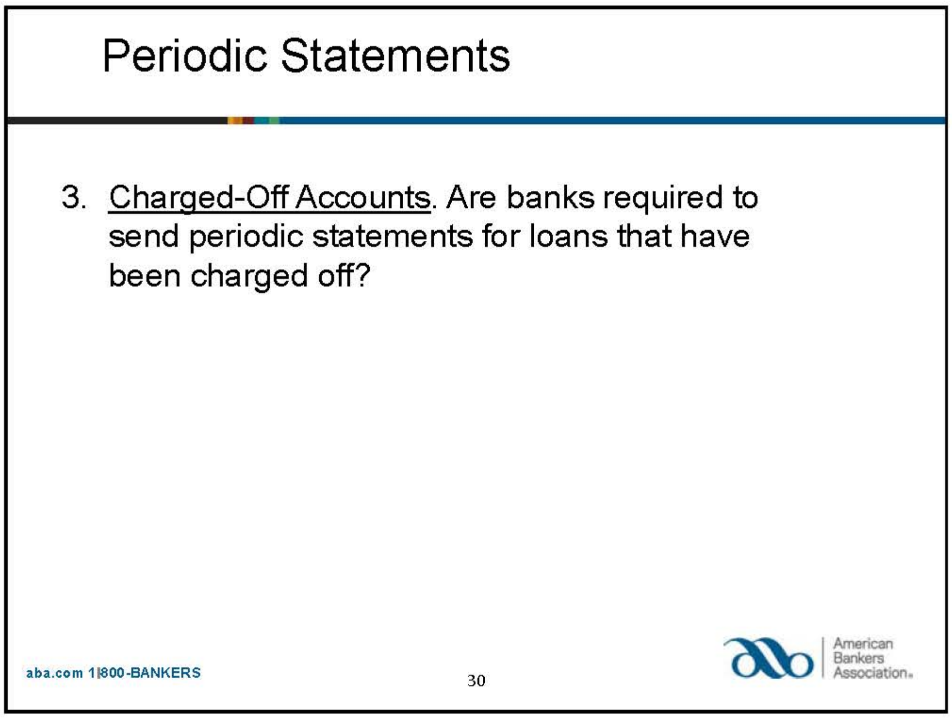
The regulations do not require the full level of E-Sign verifca-, verifications that would otherwise be needed to be E-Signed compliant. This is supposed to be a simpler process. The requirement is basically just affirmative consumer consent. So, it's up to the servicer to give the option of an electronic statement, and if the servicer decides to provide that option, there is a presumed consent concept that's in the regulation. It's actually in the, in one of the comments. So if the consumer was already receiving electronic disclosures for any account, whether it was a mortgage account or even a checking account from that servicer, the consumer is deemed to have consented to receive the periodic statement electronically.

KRISTA SHONK: What about charged off accounts? What are banks required, as Laura smiles at me across the table, what are the regulatory requirements for charged off loans?

LAURA JOHNSON: So this is again, a question that we've received numerous times. Periodic statements must be provided for a closed-end consumer credit transaction secured by a dwelling. So if the loan has been charged off, but the liens still exists, then the transaction is still secured by a dwelling and the borrower is still potentially liable.

So the servicer still must send the periodic statements. Once the lien is released, then the periodic statement obligation there would end.

KRISTA SHONK: I know that's, that's just a sidebar here, that's an area where I think some of our banks were a bit surprised last fall and, and toward the end of last year, that to learn that, that expectation existed regarding charged off accounts. So I think they're considered, perhaps still, trying to tie down a few stray cats and dogs on that one too.



LAURA JOHNSON: Right. And we've heard that level of surprise as well. And again this is another area where I think it's important to point out that if, if people are concerned about borrowers being confused, you can add information to the periodic statement to explain anything that may be confusing.

KRISTA SHONK: Okay. Well let's just stay on this slide for a minute, but so we don't need to advance the PowerPoint presentation, but we do have a couple of questions we can talk about that are not included in your slide deck under the periodic statement issue.

Let's talk a little bit about the form of the periodic statement and the safe harbor that's there, if banks use, the CFPB's model form, and so our interpretation is that servicers that do use the model form will be deemed to be in compliance with the CFPB's requirements in terms of form and content and layout, as those requirements are set forth in 1024, I'm sorry 1026.41, but to what degree is strict adherence to those forms a requirement in order to receive the safe harbor?

Because we've talked a little bit about circumstances where banks can add additional information, you know we've talked about if the loan had been accelerated or if it had accepted a lesser amount for reinstatement. We've talked about a couple of other examples today.

To what extent would adding those additional boxes, or even maybe, rearranging the boxes a bit, deem them not be able to receive that safe harbor?

LAURA JOHNSON: Sure, so, although the use of the model forms and the clauses is not required, servicers that are using them properly will be deemed to be in compliance with the regulation with regards to those disclosures. Servicers can make certain changes in the format, or the content of forms and clauses, and servicers can actually delete disclosures that are inapplicable without losing the Act's protection from liability.

One of the examples that, that I think you raised was what about certain content that's required in close proximity or grouping, can those things be shifted around? They, that information can be provided in a variety of ways. So the model forms used text within boxes, but the groupings could be done by arranging the items and using spacing between groupings and instead of boxes, other tweaks such as that are permissible. However, any rearrangement of the forms should not be so extensive that it actually affects the substance or the clarity or the, you know, the sequence of the forms.

And again, as you mentioned as well, servicers can add information to the periodic statement as long as it doesn't overwhelm or obscure the required disclosures. So there's some flexibility there.

KRISTA SHONK: Okay. And then, just before we leave this, this topic of periodic statements, let's go back to the small servicer exemption just for a moment. And we'll do that here since the definition of small servicers is included in that section on periodic statements. As you know, the small servicer exemption requires among other things, that the servicer only service loans for which it is the creditor or assignee. And, as a result of the financial crisis and some of the bank failures that have taken place over the last several years, some institutions ventured into joint venture arrangements with the FDIC whereby the bank has joint ownership with the FDIC for a pool of loans that were acquired from a failed institution. And so, the question has been posed to us in general and there's going to be a lot of specificity in terms of the variety of arrangements here, but do these types of agreement impact the bank's ability or eligibility for small servicer status?

LAURA JOHNSON: So, there's actually a comment in 2 Regulation Z, comment 41(e)(4)(iii), paragraph 1 that discusses this scenario where loans are obtained by a servicer or an affiliate as part of the acquisition of all of the assets or liabilities of a branch office of a creditor. A branch office would include an office of a depository institution that's approved of the branch by a federal or state supervisory agency. So the loans that are obtained in this type of acquisition should be considered mortgage loans for which the acquiring servicer is the creditor to which the mortgage loan is initially payable. So those loans would be counted in making the small servicer determination as if the acquiring servicer was the original creditor.

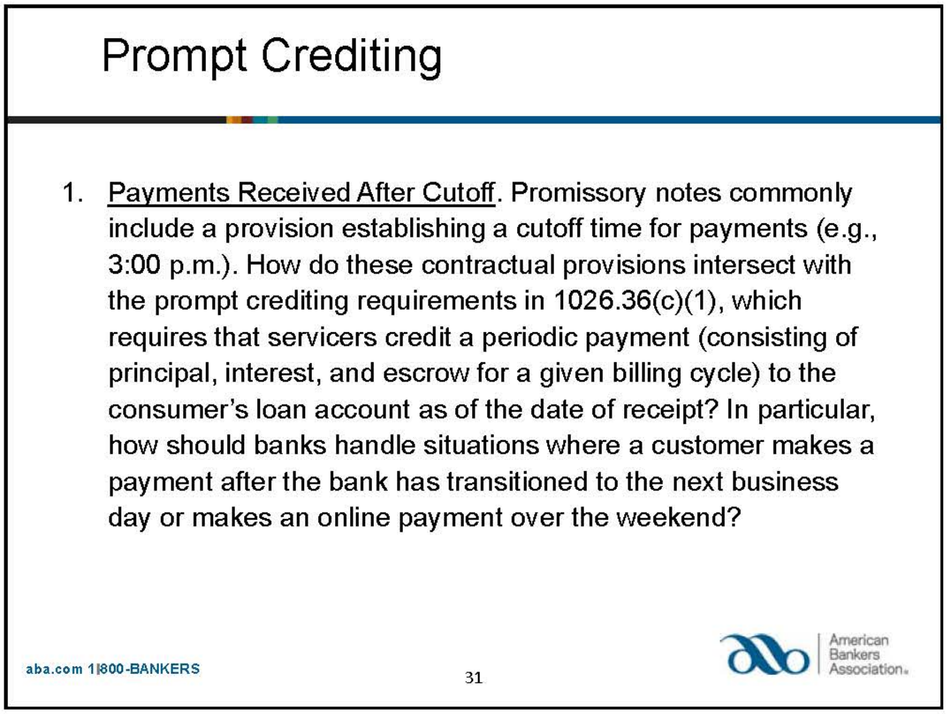
KRISTA SHONK: Even if there's a joint venture with the FDIC?

LAURA JOHNSON: Yes. They're considered, they're considered as if they were made by the acquiring servicer.

KRISTA SHONK: Okay.

LAURA JOHNSON: And one comment, I'll just throw in here because it's related to periodic statements and also related to small servicers, it's a little bit of an aside but I did want to note this because it's a question that, that we've heard before, from servicers who are eligible for the small servicer exemption, but they still want to send periodic statements of the courtesy even though they are not required to. And they've asked if those statements have to comply with the requirements under 1026.41 so you know, from our perspective, any servicer that's eligible for the small servicer exemption is certainly welcome to send statements or other accurate information to borrowers but I do want to note that those voluntary statements do not have to meet the requirements under that specific section because the small servicers are specifically exempt.

KRISTA SHONK: Thanks. I think that's helpful information. Well that's it for periodic statements, so let's move onto prompt crediting.

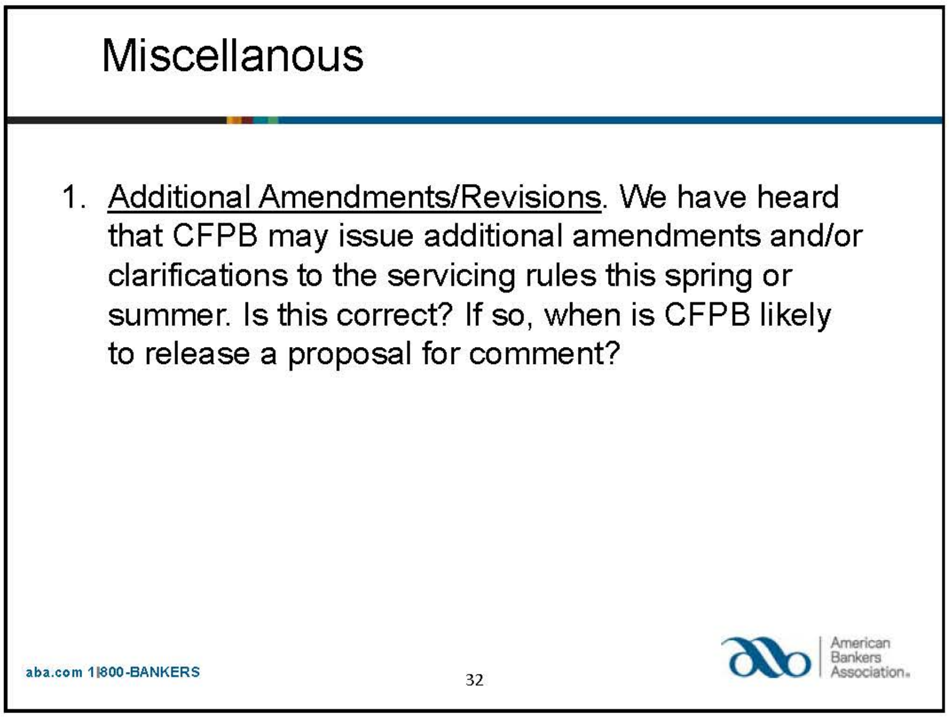


KRISTA SHONK: And this issue has just kind of bobbed around really, I'd say over the last six months and continue to come up as we've solicited questions for today's program. And the issue is, involves the crediting of payment, so there are, you know, commonly, promissory notes that include language that establishes cut off times for payments, 3 o'clock, 2 o'clock, very common. But then the prompt crediting requirement requires that servicers create or credit a periodic payment to the customer's loan account as of the date of receipt. So how does this, how should banks handle situations where a consumer comes in at, you know, 5 o'clock on a Friday, on their way home from work, the bank has already switched over to the next business day, so how, how should banks handle this type of situation in terms of crediting accounts? I guess the modern day version of that is that somebody makes their mortgage payment online on Saturday morning, as they're starting their weekend, and so the bank has already transitioned to Monday's business day. Could you just, I don't think this is anything new, but I think, given the number of questions we've received on it, perhaps it kind of bears a quick refresher?

LAURA JOHNSON: Sure, and I can just kind of walk through sort of what the, what the basic requirement is. So, under the prompt crediting requirement, as you mentioned, servicers must credit a periodic payment to the consumer's loan account, as of the date of receipt except when delaying in crediting does not result in any charge to the consumer or any negative reporting of negative information to a consumer reporting agency. In addition, servicers can specify in writing reasonable requirements for a consumer to follow in making payments.

So in determining what is reasonable, it's important to keep in mind that it should not be difficult for most consumers to make conforming payments. If a servicer establishes a reasonable cut off time, and specifies, and specifies that requirement to consumers in writing, for example, a 3 o'clock cut off time, if the consumer then makes a non-conforming payment, which would be, for example, after that time, the servicer may accept that payment and must credit it within five days of receipt.

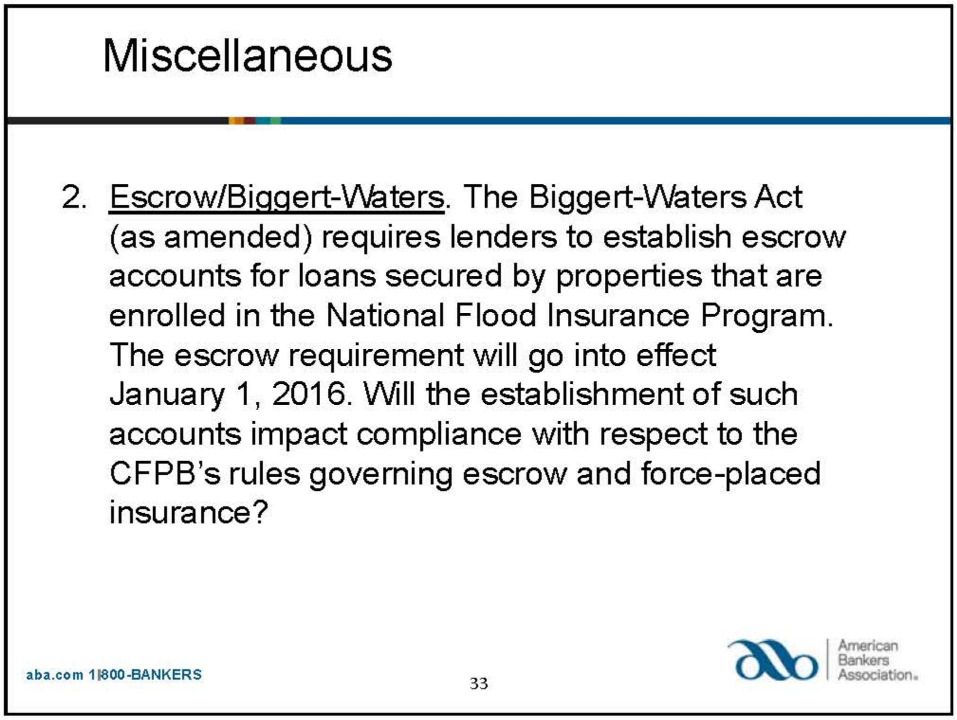
KRISTA SHONK: Moving onto the next slide.



KRISTA SHONK: Just a couple of general questions for you. Can you address the rumor mill for us? We've heard some chatter that CFPB may issue additional amendments or clarifications to the servicing rule, this spring or summer, I know there are – as we've seen today there are a variety of topics or additional guidance or clarification would be helpful, so we're just curious, is CFPB working on something? If so, can you give us some sense of when we might expect to see some, a proposal?

LAURA JOHNSON: So I can't address any specific rumors, but I will say that the Bureau is continuing to monitor the market and examine how the servicing rules are being implemented. Obviously, there have been some significant changes to the servicing rules over the past year, and there may yet be some further work to do. We're evaluating what would be the appropriate timing and scope of any additional changes to make to the servicing rules.

KRISTA SHONK: Looking even further into future, there's some questions that are coming up about Biggert-Waters Act and how some of the recent amendments to that may or may not interplay with the servicing rules.



KRISTA SHONK: And I think as folks on the phone may be aware, the amendments to Biggert-Waters require lenders to establish escrow accounts for loans that are secured by properties that are enrolled in the national flood insurance program and that escrow requirement doesn't go into effect until January of 2016. So, the question has been raised, will the requirement to establish those escrow accounts impact compliance with respect to the CFPB's rule governing escrow and forced-placed insurance?

LAURA JOHNSON: So, the Flood Disaster Protection Act requires servicers to force place insurance under certain circumstances and when that Act requires the servicer to force place insurance, that specific insurance is actually exempt from the definition of force-placed insurance under § 1024.37 in Regulation X. So, that insurance is not subject to the forced-place insurance requirements that are in that section. My understanding is that the Biggert-Waters Act does not change the circumstances in which servicers must force place insurance. So those scenarios must still be exempt from those requirements in § 1024.37. However, the escrowing of those accounts would be subject to the general requirements that we have applicable to any other escrow accounts.

KRISTA SHONK: Okay, well those are all the, the servicing questions we have for today and we have made great progress in talking about the, or talking through the various questions that our members have submitted and we actually have about 10 or 15 minutes

left and so that gives us the opportunity to turn back to Rod and Nick and they can walk through some of the additional servicing questions, I'm sorry, the origination questions as Rod's, Rod's heart skipped a beat, that we didn't include in the slide deck because frankly we didn't think we'd have time to get to them today.

So I guess, Rod, this is the bonus round, and I'll turn it over to you.

ROD ALBA: Yeah, thank you, and Nick, you know, there is a full room within a casino in Las Vegas with closed caption TV sets and security guards at the door--

NICK HLUCHYJ: Is this a question?

ROD ALBA: It is a question. That is focused on whether the CFPB will issue more origination-based regulations in 2014. Not that our members gamble, but can you give us an indication of whether you will be looking at more regulations over the course of 2014?

NICK HLUCHYJ: Well, as a long time regulator, I've been doing regulations for a long time, I think I can safely say that no final rule is the final rule. And an agency has to be a responsive to changing market conditions and new developments and, in addition, we have as we've noted many times, we have this intake portal for questions and several of those help us to identify areas where perhaps further clarity would be helpful in applying the rules. So we definitely have this on our radar screen. As to when some actual proposal may be issued, I can't say at this time.

ROD ALBA: Thank you, Nick. I will use the opportunity to throw out maybe two or three more questions. Let's, let's maybe also put an end to the, to the affiliate payment question that has drawn much attention over the past few months. Under the 4(c)(7) charges, if you pay an affiliate, even if the fees may be excluded under the 4(c)(7) exemptions, you'd have to include that payment to the affiliate into the points and fees calculation for QM and certainly for HOEPA. But what exactly is included in, when we say that the affiliate payment, is it the entire payment that is paid over to the affiliate or is it that portion that is retained by the affiliate? How is the Bureau looking at this issue?

NICK HLUCHYJ: I believe as we stated earlier, the current guidance we're providing is that the "paid-to affiliate" language, that is, actually paid to the affiliate and not something that will be eventually paid to some other party. So that's, the equivalent as saying retained by the affiliate as opposed to any amounts that the affiliate receives but does not actually retain.

And I would like to perhaps add some additional color to the question earlier on fees that are paid by the creditor and the premium pricing question, because I thought that we get many questions in this area as well, and interesting variation that came in, and your member may find this interesting, is if the creditor pays points, pays points and fees, so that they're not counted for purposes of points and fees calculation, but then says that if the consumer refinances within a three year period, that the points and fees paid by the creditor can be recaptured, that, how does that effect, let's say the qualified mortgage determination? And the answer to that question is that if the creditor is going to recapture those points and fees, then they would be considered to be a prepayment penalty under the (b)(1)(v) prong of the points and fees test.

Although there's an exclusion there for third party, bona fide third party charges that are paid through the creditor that are waived and that can be recaptured within a three year period. By definition, points and fees are not bona fide third party fee charges. So if the creditor is actually making the payments for points and fees, if they're to be recaptured within that 36 month period, they would be considered to be a prepayment penalty in effect it would be a wash. They wouldn't be excluded from the points and fees calculation.

ROD ALBA: Okay. Thank you for that clarification. I think we'll reduce that to writing. We appreciate that, Nick. The, the additional question also relating to QM, in certain instances, with consumer debt, particularly the famous or infamous American Express credit cards, outstanding consumer loans do not have a monthly minimum payments that are lifted. Technically, the entire balance in an American Express credit card is due in full on a monthly basis. The creditor's certainly the, when, when repaying on the credit card allow monthly payments, so should the originating entity in an ATR/QM covered transaction, should, should we figure in the entire balance that is showing on the report into the DTI ratio? Or should we convert the debt into some sort of monthly payment calculation?

NICK HLUCHYJ: Well they, there's not a lot of guidance on the ATR portion as it is. The section under current debt obligations at (c)(2)(vi), that deals with current debt obligations mentions revolving accounts but then doesn't say much more about them but then it doesn't say much more about them. However there is guidance provided in Appendix Q for purposes of the QM, and there in Section III.3, it states that if there is an outstanding balance on an account but there's no specific monthly minimum payment, and so if there is a monthly payment, that's what you would use, that's specified, but if there isn't any one, you would use the greater of 5% or $10 for purposes of computing the monthly payment on that balance.

ROD ALBA: Great. So great. So even outside of QM, certainly the use of Appendix Q would be allowed, and it's certainly allowed by the Bureau?

NICK HLUCHYJ: That's correct.

ROD ALBA: I'll give you the next question, and I believe the last question, before we close. Can we, under the LO Compensation Rules, can lenders pay bonuses or incentive compensation to mortgage loan originators from venture-wide profits that exclude mortgage profits? So the banks would be separating the mortgage profits from all other types of profits to pay these bonuses with, with the logic being that you wouldn't have a proxy because none of the payments would be tied to, if you will, mortgage related activities.

NICK HLUCHYJ: Thanks for this question, Rod. I did discuss this with our loan originator experts. As you know, we tend to specialize in particular areas, and while all of us have a general familiarity with the requirements, some of us have a much more specialized and refined understanding of the requirements. If the profits, the profits are segregated so that the mortgage-related profits are not included in the source of the payments to the loan originator, that is not something that's related to the terms of the transaction and therefore, would not be subject to the limitations on loan originator compensation.

ROD ALBA: Okay, thank you. With that, Krista, I will turn the mic back to you.

KRISTA SHONK: Okay. Before we turn things back to Tim from KRM, just a couple of notes for everyone on the call. You can see on the last page of this slide deck, there is a link to the mortgage page of the ABA website. If you're not familiar with the information on that site, I would encourage you to take a look at it. It includes a variety of materials that Rod and I have put together. There are a number of very detailed outlines of the CFPB rules. There are also several FAQs that may be of assistance to you. I should note that we will be, take a look at them now, but we will be updating them based on the information that Nick and Laura shared today, so look at it today but then check back for the new information. There's also a variety of other mortgage-related materials that may be of assistance to you.

And so finally, just Nick and Laura, thank you very, very much for being here today, and I know you both put a lot of time into it. We had a number of, of conference calls to prepare for the program today, and we really appreciate it.

LAURA JOHNSON: Thanks for inviting us.

NICK HLUCHYJ: Yes, thank you.

KRISTA SHONK: And Tim, we'll turn things back to you for a wrap-up.

TIM: All right. Well, thank you so much, Krista, and that concludes today's ABA Briefing/Webcast, Mortgage Q&A with the Consumer Financial Protection Bureau. Today's live briefing includes a 7-day complimentary access to the streaming recording of this program, and you will receive instructions, they will be sent to you within 2 days from today.

When I end the briefing, your computer will go to an online evaluation form for today's program. We'd very much appreciate your comments and suggestions so that we can bring you future quality briefings. So we encourage you to participate on that online evaluation. If you're listening to the telephone audio only, there are instructions in your handout materials as well.

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