The Impact of the Mortgage Reform & Anti-Predatory Lending Act On The Conventional Residential Lending Industry

© Richard D. Vetstein, Vetstein Law Group,
Framingham, MA

The new ***Mortgage Reform and Anti-Predatory Lending Act***, buried in the fine print of the much publicized **Dodd-Frank Wall Street Reform and Consumer Protection Act** contains strict new rules aimed at preventing another sub-prime mortgage collapse.

Overview: What Is The Impact To Mortgage Lenders and Originators?

The Mortgage Reform and Anti-Predatory Lending Act certainly changes the regulatory landscape for mortgage originators who focused on high-risk, sub-prime lending, setting tougher new standards and creating new federal remedies for consumers victimized by deceptive and predatory lending. Stripped down, the Act puts the onus on mortgage lenders and originators to ensure, based on verified and documentation information, that borrowers can afford to repay the loans for which they have applied. Pretty novel idea, huh?

The new law essentially codifies good underwriting practices by requiring consideration of a borrower's "credit history, current income, expected income the consumer is reasonably assured of receiving, current obligations, debt-to-income ratio or the residential income the consumer will have after paying non-mortgage debt and mortgage-related obligations, employment status, and other financial resources other than the consumer's equity in the dwelling or real property that secures repayment of the loan."

I don't see anything in these rules that a financially prudent lender wouldn't have already implemented in its underwriting processes. Lenders should not be placing borrowers into loans they are doomed to fail.

I'm sure these new rules will result in a few more disclosures and forms, but I don't see this making a major impact on the conventional residential lending industry. If mortgage professionals think otherwise, I'd love to here from you. Well, onto the details:

<u>New Minimum Mortgage Affordability Standards</u>

The new law essentially outlaws many of the characteristics of the classic sub-prime, predatory mortgage loan, by requiring that:

- The mortgage provides that regular periodic payments do not result in an increase of the principal balance of the loan or allow the consumer to defer repayment of principal.

- The mortgage does not result in a balloon payment (a scheduled payment that is more than twice as large as the average of earlier scheduled payments).
- The income and financial resources relied upon by the lender have been verified and documented.
- The underwriting process for a fixed loan is based on a payment schedule that fully amortizes the loan over the loan term, taking into account all applicable costs.
- The underwriting process for an adjustable rate loan is based on the maximum rate permitted under the loan for the first five years and a payment schedule that fully amortizes the loan over the loan term, taking into account all applicable costs.
- The mortgage complies with guidelines and regulations related to ratios of total monthly debt to total monthly income or alternative measures of a borrower's ability to pay.
- The mortgage has total points and fees amounting to no more than 3 percent of the total loan amount.
- The term of the loan does not exceed 30 years.

It would appear that this new law would prohibit so-called "no doc" "no income verification" loans.

The new law also imposes on lenders a duty to verify amounts of income or assets that the lender relies upon to determine the consumer's ability to repay the loan. Again, a novel idea…In order to "safeguard against fraudulent reporting," lenders are now required to use IRS transcripts of tax returns.

New Loan Origination Standards

The new law requires that lenders be qualified and registered as mortgage originators under the applicable federal and state laws. The significance of this registration procedure is that all loan documents will require the inclusion of the mortgage originator's unique identifier, which is to be provided by the National Mortgage Licensing System and Registry. This will enable tracking of the bad guys.

"Steering Incentives" Prohibited

The Dodd-Frank Act will prohibit lenders from "steering" borrowers into more costly loans. It will prohibit mortgage originators from mischaracterizing the credit history of a consumer or the residential loans available to the consumer for purposes of making the loan. Mortgage originators are also prohibited from discouraging consumers from seeking a residential mortgage loan from another lender when the former is unable to suggest, offer, or recommend a loan that is not more expensive.

Predatory Loans Banned

Mortgage originators are prohibited from steering consumers to residential mortgage loans that have "predatory characteristics or effects." "Predatory characteristics," include equity stripping, excessive fees, or abusive terms.

Yield-Spread Premium Bonuses Outlawed

The Dodd-Frank Act also imposes new compensation limitations by prohibiting yield-spread premium bonuses, a practice, regulators argue, tends to increase the total cost of the loan to the borrower. Yield spread premiums (YSPs) are fees paid by a lender to a mortgage originator for placing a loan in a certain loan program.

Additional Liability for Mortgage Originators

The Act imposes liability on mortgage originators who fail to comply with these new minimum standards. It provides the penalty of triple damages plus the costs of suit and reasonable attorneys' fees. Watch out for class actions here!