

Mortgage Banking Update

PATTON BOGGS LLP | OCTOBER 12, 2009

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TWO MORE FAQs ON THE NEW RESPA RULE

On October 7, the [Department of Housing and Urban Development \(HUD\)](#) issued two more FAQs on the new rule under the Real Estate Settlement Procedures Act (RESPA) to be implemented on January 1, 2010. One FAQ is a revised version of a previously withdrawn FAQ regarding prepayment penalties. The other FAQ addresses a concern that the revised HUD-1 does not sufficiently provide for the tax deductibility of points.

Prepayment Penalty Issue

Under the new RESPA rule, both the good faith estimate (GFE) and HUD-1/1A provide for the disclosure of basic loan terms, including whether the loan has a prepayment penalty. The initial version of the FAQs issued on August 13 addressed a feature of FHA loans under which it is common for the borrower to be required to pay interest through the end of the month when a prepayment in full occurs other than on the due date of a periodic payment. This is because interest is accrued on a monthly basis with FHA loans. One FAQ addressed whether the requirement to pay interest after a prepayment in full must be disclosed as a prepayment penalty in the GFE and HUD-1/1A. HUD advised in the FAQ that the requirement is not a prepayment penalty and, thus, should not be disclosed as a prepayment penalty in the GFE or HUD-1/1A.

In the August 19 version of the FAQs, the FAQ addressing the prepayment penalty issue was withdrawn without explanation. Apparently, HUD withdrew the FAQ after discussing the matter with the Federal Reserve Board. In the commentary to the Truth in Lending Act (TILA) rules, the Fed takes the position that a requirement to pay interest after the prepayment in full of a mortgage loan is a prepayment penalty.

As addressed in the [September 28](#) and [October 5](#) editions of the Mortgage Banking Update, the Fed position presented an issue under TILA rules that went into effect on October 1. The rules create a new class of mortgage loans known as higher-priced mortgage loans (HPMLs). Subject to exceptions, a loan is an HPML if it is secured by the consumer's principal dwelling and the annual percentage rate equals or exceeds a certain threshold. The threshold is 1.5 percentage points above the applicable average prime offer rate (or 3.5 percentage points above such rate for a subordinate-lien loan). The average prime offer rate is computed by the Fed. Based on the rate in effect for the week of October 12, a fixed-rate loan with a 30-year term would be an HPML if the annual percentage rate was 6.43 percent or higher. Because of the relatively low annual percentage rate threshold, industry groups believe that many FHA loans will be HPMLs, which presents an issue given the prepayment penalty restriction applicable

LOOKING AHEAD:

How Will FHA Reforms Impact the Mortgage Industry?

October 14

Webinar Topic: Addressing Changes at FHA

Time: 1:00-2:00 p.m. EST

Patton Boggs participants:

Richard Andreano, Heather

Hutchings

Space is Limited

LBA's Bank Counsel

Conference

November 13

Location: The Ritz Carlton, New Orleans

Topic: RESPA Reform: The Latest from Washington, DC

Time: 10:35-11:35 a.m. CST

Patton Boggs participant:

Richard Andreano

to HPMLs and the Fed's position that a requirement to pay interest after the prepayment in full of a mortgage loan is a prepayment penalty.

In a September 29 letter labeled as an "official interpretation," the Fed's director of the Division of Consumer and Community Affairs advised that the commentary provision under which a requirement to pay interest after a full prepayment is a prepayment penalty does not apply to FHA loans. The director rendered this advice on the grounds that the "commentary on this issue does not expressly address this issue in the context of monthly interest accrual amortization". (Please see the [September 28](#) and [October 5](#) editions of the Mortgage Banking Update for more information on the TILA issue.)

In the October 7 version of the FAQs, HUD included a revised FAQ regarding the disclosure of whether the loan has a prepayment penalty. Citing the September 29 letter from the director, HUD advises that the requirement with an FHA loan to pay interest after the date of a full prepayment is not a prepayment penalty and, thus, does not have to be disclosed as a prepayment penalty in the GFE or HUD-1/1A.

Deductibility of Points

The new RESPA rule revises the approach to the disclosure of lender and broker compensation and the disclosure of points and yield spread premiums. All compensation received by the broker and lender are included in a single disclosure on Line 801 of the HUD-1/1A labeled "Our origination charge". Line 802 of the HUD-1/1A is for the disclosure of "Your credit or charge (points) for the specific interest rate chosen." Line 802 would include any points paid by the borrower, or any yield spread premiums and other lender-paid broker compensation or closing cost payments. Such lender payments would be shown as a credit to the borrower from the lender. The revised approach presents an issue as to whether points will be sufficiently designated as such in the HUD-1/1A to meet Internal Revenue Service (IRS) requirements for the consumer to be able to deduct the points for tax purposes. Among other criteria, the IRS requires that the points be clearly shown on the HUD-1/1A as points paid for the mortgage loan.

A new FAQ provides that "A loan originator may designate any origination point paid on page 2 of the HUD-1 Line 801. The designation should follow "Our Origination Charge" either by adding the language "Includes Origination Point" (___% or \$__) or by placing an asterisk (*) and adding the language at the bottom of the page."

Unfortunately, this advice appears to conflict with the new RESPA rule. The new RESPA rule provides that Line 801 "is used to record "Our origination charge," which includes all charges received by the loan originator, except any charge for the specific interest rate chosen (points)." HUD will need to address the FAQ, which provides for disclosing the points in Line 801, and the RESPA rule, which provides that points may not be included in Line 801.

DID YOU KNOW

- State Regulatory Registry, LLC, the entity that owns the Nationwide Mortgage Licensing System (NMLS), released the first edition of its “NMLS Policy Guidebook for Licensees” during the week of October 5. The stated purpose of the guidebook is to assist licensees and other users of the NMLS with understanding certain policies related to the system. We encourage licensees to review the guidebook to determine whether their NMLS records are consistent with the instructions set forth in that manual. To the extent that a licensee’s NMLS record is not entirely consistent with the guidebook, licensing managers are encouraged to route proposed changes through appropriate internal channels to ensure that any such modifications to the NMLS record will not adversely impact the licensee’s operations and/or its regulatory compliance efforts.

EXECUTIVE ORDER ON FEDERAL AGENCY ROLE IN ENERGY AND THE ENVIRONMENT

On October 5, 2009, President Obama issued a sweeping executive order directing federal agencies to “increase energy efficiency; measure, report and reduce their greenhouse gas emissions from direct and indirect activities;... eliminate waste, recycle and prevent pollution...” The primary thrust of this order seems to be federal agency buildings and vehicles but it could be applied to loan, loan insurance and loan guarantee programs. Neither the [White House](#), [Department of Housing and Urban Development \(HUD\)](#), nor any other lending, or loan guaranteeing/insuring federal agency has publicly addressed the possibility of forcing borrowers to go “green” in order to obtain federal financial assistance, but pressure to show large increases in energy efficiency and corresponding decreases in pollution and greenhouse gas emissions could move HUD toward imposing “green” standards on federally-assisted projects. This could have a sweeping impact on a number of HUD programs, especially the FHA single-family and multifamily insurance programs.

Some indication of HUD’s intentions in this respect should be apparent by early January, if not before, since all federal agencies must report greenhouse gas percentage reduction targets by then. We will keep you informed of developments concerning this order. For more information, please contact [Tim Vanderver](#) at 202.457.6074 or tvanderver@pattonboggs.com.