Comments of

Massachusetts Mortgage Bankers Association
on
Board of Governors of the Federal Reserve System
Proposed Rule amending Regulation Z
74 Fed. Reg. 43232, August 26, 2009

DOCKET NO. R-1366

December 24, 2009

Jennifer J. Johnson
Secretary – Board of Governors
Federal Reserve System
20th and Constitution Avenue, NW
Washington, DC 20551

Dear Ms. Johnson :

The Massachusetts Mortgage Bankers Association appreciates the opportunity to provide comment on certain parts of the Federal Reserve System proposed rule amending Regulation Z 74 Fed. Reg. 43232, August 26, 2009. For the purpose of many of the broad based comment on the proposed rule including all of the new *Disclosure proposals,* the MMBA would defer much of the specific comments on portions of the rule to the national Mortgage Bankers Association of America and to the National Association for Mortgage Brokers as submitted. In addition, there are many well thought out and well prepared comments on *Originator Compensation* from the aforementioned that we, likewise would ask for appropriate consideration however, the MMBA would reserve additional comment as outlined below

For the purpose of the Massachusetts mortgage industry, we would draw your attention to the three specific comments as they pertain to the propose rule:

1. **Delay implementation of any final rule:**
   With regard to the overall timing of the proposed initiative, the MMBA would strongly advocate for the delay of any implementation of the final rule until after Congress has acted on proposed legislation that would create a new Consumer Protection Agency and until after the mortgage industry would have the opportunity to react and adjust to the now current market conditions. In addition, the mortgage lending industry is still reeling from the guideline adjustments necessary to adapt to the new mortgage model including adaptation through TARP, HAMP, MDIA / TILA, RESPA / HUD 1 as well as the many investor and Fannie Mae, Freddie Mac and Ginnie Mae guideline changes.

   The Massachusetts mortgage industry like the rest of the nation is struggling to maintain a sustainable business model while adjusting to all of the industry changes at this time. Finally, concluding a comment period on Christmas Eve (December 24, 2009) adds to the difficulty that a struggling industry has to adjusting to the market and participating in the regulatory process.

2. **Annual Percentage Rate:**
   With regard to the Board's interest in clarifying the Annual Percentage Rate and redefining the Finance Charge to a broader "Interest and Settlement Charges", and the timing of disclosures:

Until the requirements of HUD's recent rule making (73 FR 68204) are fully understood by the mortgage lending industry, (including the recently released Frequently Asked Questions and Settlement Cost Booklet) it will be nearly impossible for those involved in process to know which fees paid by the consumer will fall into which of the categories established by HUD (for purposes of placement on the Good Faith Estimate and Final HUD-1, for tolerance purposes, and with respect to any violations, consequent potential reimbursement status), and to cross reference them to the new categories established by the Federal Reserve in this Proposed Rule making (for Finance Charge/APR calculation, for re-disclosure purposes and consequent potential TILA violations).

The Proposed Rule would expand the fees reflected in the APR calculation to include fees imposed by the creditor related to real estate purchases, even if the creditor allows the consumer to choose the third party provider. Commentary to the Proposed Rule indicates that this is intended to eliminate the 'some fees in; some fees out' disclosure that now exists. However, under the Proposed Rule, an increase in one of those fees would potentially trigger a new TILA disclosure and a consequent three day delay in closing, even if the fee is one of the borrowers own choosing. This categorization is not compatible with the existing HUD Rule in which categories of fees are permitted to increase between application disclosures and final closing disclosures based on tolerance groups, essentially because the borrower does have the choice of provider. Unlike the Board's reasoning in this Proposed Rule, an increase in such a fee (borrower chosen, unlimited variance permitted) has no impact on the lender's disclosure responsibilities nor the borrower's closing date. While the commentary addresses the concern of some groups, that consumers have been 'surprised at closing' by changes in loan *terms*, they should not be surprised to see an increase in a cost where they have selected the provider. This Proposed Rule should recognize the difference between who selects the provider and coordinate with the new Rules regarding RESPA compliance.

For these, among other reasons, we urge that the Federal Reserve to delay any rule making, and to reissue a Proposed Rule regarding the calculation, renaming and timing of disclosures related to the Finance Charge and Annual Percentage Rate until the effects of the rule making by HUD are absorbed by the lending industry. At a minimum, we suggest a new Proposed Rule issue after the conclusion of HUD's recommended 120 day 'restraint of enforcement' period to allow lenders to absorb the impact of HUD's new rule making and the issuance of Frequently Asked Question guidance.

3. **Loan Originator Compensation:**

With regard to loan originator compensation, both the national MBA and NAMB have provided very detailed comment on the role of the mortgage originator, appropriate definitions and loan scenarios highlighting appropriate compensation strategies **(Attached).** All of this should be taken into consideration before issuing a final rule.

From October 2007 until January 2008, the Commonwealth of Massachusetts' Attorney General, Martha Coakley worked throughout consumer advocacy and industry trade associations in concluding that widespread acts and practices in the area of residential mortgage lending unfairly harmed consumers of the Commonwealth. Therefore, the Massachusetts Attorney General updated and amended the 1992 mortgage broker and lender regulations to address certain consumer problems when they sought to obtain mortgage loans for purchase or refinance. The Attorney General's regulations defined unfair or deceptive acts or practices in mortgage lending as prohibited by MGL 93A Sect 2(a) and 940 CMR 8.00 **(Attached)**.

The Attorney General's regulations under Chapter 93A and subsequent FAQ's **(Attached)** address many issues affecting the mortgage transaction including mortgage disclosures (8.05) and prohibited practices (8.06). Moreover, the Attorney General's regulations specifically addresses a broker or loan originator being prohibited to make or arrange a loan that is not in the borrower's interest (17)

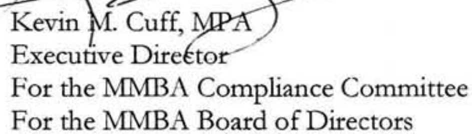
which, likewise specifically includes a prohibition against a mortgage broker or originator placing their financial interest in conflict with the loan terms and the consumer's interest.

The MMBA offers you both the Attorney General Regulations and subsequent FAQ's (specifically FAQ pages 5 – 14 addressing broker / loan originator compensation) as standing regulation and current business practice of the Commonwealth of Massachusetts since January 2008.

We believe that the Massachusetts Attorney General has determined that a broker / loan originator compensation through the use of Yield Spread Premium that does not place a conflict between compensation and the borrower's interest to be an acceptable use of the model.

The MMBA again appreciates the opportunity to comment on the proposed amendments to Regulation Z. We look forward to working with the Federal Reserve Board in any way on improving the mortgage process for consumers, a matter of utmost importance to our industry. Should you have any questions, or to discuss any of the opinion as outlined within the comment further, please do not hesitate to contact me at 617.570.9114.

Sincerely,



Kevin M. Cuff, MPA
Executive Director
For the MMBA Compliance Committee
For the MMBA Board of Directors

The Massachusetts Mortgage Bankers Association (MMBA) is the Commonwealth's trade association representing the real estate finance industry. Founded in 1974, the MMBA is the largest mortgage association in New England and is one of the most successful in the country. The association works to ensure the continued strength of the Commonwealth's residential real estate markets; to expand homeownership prospects through affordability; and to extend access to affordable housing. The MMBA promotes fair and ethical lending practices and promotes excellence and integrity among real estate finance professionals through a wide range of educational programs, advocacy and industry-wide publication. Its membership of approximately 400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, insurance companies, appraisers, etc. and others in the mortgage lending field. For additional information, visit MMBA's Web site: www.massmba.com

[940 CMR Part 8, December 18, 2007]

ATTORNEY GENERAL REGULATIONS UNDER CHAPTER 93A MORTGAGE LENDERS AND BROKERS

8.01: Purpose

In 1992, the Attorney General of Massachusetts promulgated 940 CMR 8.00 relating to mortgage lenders and mortgage brokers pursuant to the Attorney General's authority in M.G.L. c. 93A, § 2(c). These regulations were designed to protect Massachusetts consumers seeking residential mortgage loans for home improvements and other purposes, other than for the purchase or initial construction of residential property or open-end home equity lines of credit, and to ensure that the mortgage industry is operating fairly and honestly by means of legitimate and responsible business acts and practices that are neither unfair nor deceptive.

In 2007 it is now clear that certain widespread acts and practices in the area of residential mortgage lending continue to unfairly harm consumers. The Attorney General, therefore, has updated and amended the 1992 mortgage broker and lender regulations to address problems experienced by consumers when they seek or obtain mortgage loans for the purchase or initial construction of residential homes, or when consumers refinance. The regulations will continue to address problems experienced by consumers when they obtain mortgage loans for purposes other than purchase money financing and initial construction, including the purpose of refinancing an existing loan.

8.02: Scope

The Attorney General's regulations define unfair or deceptive acts or practices. They are not intended to be all inclusive as to the types of activities prohibited by M.G.L. c. 93A, § 2(a). Acts or practices not specifically prohibited by 940 CMR 8.00 are not necessarily consistent with Chapter 93A or otherwise deemed legitimate by the absence of regulation here. 940 CMR 8.00 is designed to supplement existing regulations. All references in 940 CMR 8.00 to statutes and other regulations shall include amendments made to such statutes and regulations after the promulgation of 940 CMR 8.00.

940 CMR 8.00 shall cover any mortgage lender or broker advertising or doing business within Massachusetts, regardless of whether or not the lender or broker maintains an office in Massachusetts.

940 CMR 8.00 applies to all residential mortgage loan transactions in the Massachusetts, as more particularly defined in these regulations, except that it does not apply to either (i) reverse mortgages governed by G.L. c. 167E, § 7, or (ii) open-end home equity lines of credit. Reduced interest rate mortgages originated under the auspices of affordable housing programs which are administered by state, quasi-public, or local government entities are also excluded.

8.03: Definitions

"Advertisement" (including the terms "advertise" and "advertising") shall be defined in a manner which is consistent with the definition provided by the applicable sections of the Attorney General's Retail Advertising Regulations, 940 CMR 6.00, and means any oral, written, graphic, or pictorial statement made by a mortgage broker or lender in any manner in the course of the solicitation of business. Advertisement includes any representation made in a newspaper, magazine, or other publication or on the Internet, radio or television or contained in any notice, handbill, sign, billboard, banner, poster, display, circular, pamphlet, catalog, or letter. Advertisement includes any representation disseminated or accessible within Massachusetts if the advertisement is directed to consumers in Massachusetts.

"Bait advertising" means an offer to procure, arrange, or otherwise assist a borrower in obtaining a mortgage on terms which the broker or lender cannot, does not intend, or want to provide, or which the broker or lender knows cannot be reasonably provided. Its purpose is to switch borrowers from buying the advertised mortgage loan product to buying a different mortgage loan product, usually at a higher rate or on a basis more advantageous to the broker or lender.

"Borrower" means any natural person seeking, using, or paying for, directly or indirectly, the services of a mortgage lender or broker in connection with a mortgage loan.

"Broker fee" means any money, compensation, commission, fee, charge or other valuable consideration directly or indirectly imposed by a mortgage broker for the broker's services in negotiating, placing, finding, or otherwise assisting a borrower in obtaining a mortgage loan. The term broker fee does not include a fee charged by the lender (such as a commitment fee or a lock-in fee), wages or commissions paid to an employee of the mortgage broker or mortgage lender by his or her employer, nor does such term include bona fide and reasonable payments to be remitted to third party service providers, such as appraisal fees or fees for credit reports or payments or remittances to the mortgage lender.

"Clear and conspicuous" (including the terms "clearly and conspicuously") shall be defined in a manner which is consistent with the definition provided by the applicable sections of the Attorney General's Retail Advertising Regulations, 940 CMR 6.00. 940 CMR 6.01 provides that clear and conspicuous (including the terms "clearly and conspicuously") shall mean that:

> the material representation being disclosed is of such size, color, contrast, or audibility and is so presented as to be readily noticed and understood by a reasonable person to whom it is being disclosed.

Further, without limiting the requirements of the preceding sentence, regulation 940 CMR 6.01 states that a representation in an advertisement is not clear and conspicuous unless:

> 1. for a printed, written, typed or graphic advertisement, such material representation appears in type which is at least one-third the size of the largest type of information which it modifies and is a minimum of eight point type;
>
> 2. for the video portion of a television advertisement, such material

representation:

a. is displayed in type not less than 14 scan lines in height;

b. contains letters of a color or shade that noticeably contrast with the background, and the background does not consist of colors and/or images which obscure or detract attention from the representation or are disparaging to its meaning or importance; and

c. appears on the screen for a duration equal to at least one second for every three words of the material representation but not less than a total of five seconds.

3. for a radio advertisement or the audio portion of a television advertisement, such material representation complies with the requirements of 940 CMR 6.01(c).

"Commissioner" means the Commissioner of Banks.

"Commitment for mortgage loans" (or the word "commitment") means an oral or written agreement to loan or to advance funds for a mortgage loan. A commitment can specify a loan amount, repayment terms, interest rate or conditions necessary to close the loan.

"Contractor" or "home improvement contractor" means any person who owns or operates a residential contracting business or who undertakes, offers to undertake, purports to have the capacity to undertake, or submits a bid for, by him or herself or through others, residential contracting work as defined in M.G.L. c. 142A.

"Mortgage broker" or "broker" means any person, who for compensation or gain, or in the expectation of compensation or gain, directly or indirectly negotiates, places, assists in placement, finds, or offers to negotiate, place, assist in placement or find mortgage loans on residential property for others, or as otherwise defined by M.G.L. c. 255E, § 2 or by the Commissioner. Notwithstanding anything to the contrary in these regulations, the following persons shall not be deemed to be a mortgage broker:

(a) any person who is exempt from the licensing requirements of M.G.L. c. 255E, § 2; provided, however, that individuals who work for or on behalf of brokers that are licensed pursuant to G.L. c. 255E, § 2, shall not be exempt from these regulations; and

(b) any financial institution which is regulated by a federal and/or state bank regulatory agency and which, directly or indirectly, negotiates, places, assists in placement, finds, or offers to negotiate, place, assist in placement or find mortgage loans on residential property for a direct or indirect affiliate or subsidiary of such financial institution.

"Mortgage lender" or "lender" means any person engaged in the business of making mortgage loans or issuing commitments for mortgage loans, including, but not limited to, mortgage lenders licensed or regulated by M.G.L. c. 255E, §2 or the Commissioner, and shall include all individuals who work on behalf of such lenders.

"Mortgage loan" or "loan" means a loan to a natural person primarily for personal, family or household use secured wholly or partially by a mortgage on residential property, or as otherwise defined by M.G.L. c. 255E or the Commissioner, and shall include loans to refinance a mortgage. "Mortgage loan" or "loan" shall not include either (i) reverse mortgages governed by G.L. c. 167E, § 7, or (ii) open-end home equity lines of credit.

"No Income Loan Product" means a mortgage loan where: (i) in making its decision whether to underwrite the loan or extend credit, the mortgage lender does not account for or consider, in any manner whatsoever, the prospective borrower's income or employment status, and (ii) that fact is set forth in the lender's written underwriting or loan origination policies governing its No Income Loan Product.

"Person" means a natural person or organization including a corporation, partnership, association, cooperative or trust or any other legal entity.

"Point" means an origination fee, finder's fee, or other fee, premium, service charge, or any other charge calculated as a percentage of the principal amount of the loan or a percentage of the amount financed, however such point may be called, which is charged by a mortgage lender at or before the time the mortgage loan is made as additional compensation for the mortgage loan, or as otherwise defined by M.G.L. c. 183, § 63 or the Commissioner. A point does not include:

(a) bona fide and reasonable fees for actual services performed including, but not limited to, attorney's fees, appraisal fees, credit reporting fees, private mortgage insurance premiums, and title insurance premiums or mortgage broker fees; or

(b) a charge which is credited to closing costs or other costs relating to such loan.

"Residential property" means real property located in Massachusetts having thereon a dwelling house with accommodations for four or fewer separate households and occupied, or to be occupied, in whole or in part by the obligor of the mortgage debt, or as otherwise defined in M.G.L. c. 255E.

8.04: Advertising Practices

(1) It is an unfair or deceptive act or practice for a mortgage broker or lender to make any representation or statement of fact in an advertisement if the representation or statement is false or misleading or has the tendency or capacity to be misleading, or if the mortgage broker or lender does not have sufficient information upon which a reasonable belief in the truth of the representation or statement could be based.

(2) It is an unfair or deceptive act or practice for a mortgage broker or lender to advertise without clearly and conspicuously disclosing its business name, and if required to be licensed pursuant to M.G.L. c. 255E, the words "broker" or "lender", as applicable, and the license number.

(3) It is an unfair or deceptive act or practice for a mortgage broker to represent in any advertisement that the mortgage broker will fund a mortgage loan.

(4) It is an unfair or deceptive act or practice for a mortgage broker or lender to engage in bait advertising or to misrepresent (directly or by failure to adequately disclose) the terms, conditions or charges incident to the mortgage loan being advertised in any advertisement. Violations of 940 CMR 8.04(4) shall include, but shall not be limited to:

(a) the advertisement of "immediate approval" of a loan application or "immediate closing" of a loan or words of similar import, such as "instant closing";

(b) the advertisement of a "no point" mortgage loan when points are required or accepted by the lender as a condition for commitment or closing;

(c) the advertisement of an incorrect specific number of points required for commitment or closing;

(d) the advertisement through terms such as "bad credit no problem" or words of similar import or that an applicant will have unqualified access to credit without clearly and conspicuously disclosing the material limitations on the availability of credit that may exist, such as:

1. requirements for the availability of credit (such as income);

2. that a higher rate or more points may be required for a consumer with bad credit; and

3. that restrictions as to the maximum principal amount of the loan offered may apply.

(e) the use of "avoid foreclosure" or words of similar import in an advertisement unless the advertisement also clearly and conspicuously discloses, that:

1. the borrower must refinance the mortgage in default and/or take a new mortgage loan;

2. the borrower may be required to pay interest rates significantly higher than what other

borrowers not facing foreclosures might pay; and

3. the warning that "you may lose your home if you cannot make all the payments or if you miss any of the payments on this loan."

(5) It is an unfair or deceptive act or practice for a mortgage broker or lender who advertises any finance terms to fail to comply with the applicable state and federal advertising laws, Truth-in-Lending laws, M.G.L. c. 140D, §1, et seq., and 15 U.S.C. §1601, et seq., and any regulations promulgated thereunder.

8.05: Mortgage Disclosures

(1) It is an unfair or deceptive act or practice for a mortgage broker or mortgage lender to fail to make any disclosure, or fail to provide any document, to a consumer required by and at the time specified by any applicable state or federal law, regulation or directive.

(2) It is an unfair or deceptive act or practice for a mortgage broker or lender to conceal or to fail to disclose to a borrower any fact relating to the loan transaction, disclosure of which may have influenced the borrower not to enter into the transaction with the broker or lender.

(3) It is an unfair and deceptive act or practice for the mortgage broker or lender to fail to take reasonable steps to communicate the material facts of the transactions in a language that is understood by the borrower. Reasonable steps which shall comply with this regulation may include but shall not be limited to:

(a) using adult interpreters; and

(b) providing the borrower with a translated copy of the disclosure forms required by any applicable state or federal law, regulation or directive, in a language understood by the borrower.

(4) It is an unfair or deceptive act or practice for a mortgage lender to fail to give to the borrower legible copies of the mortgage deed, promissory note, and the settlement statement when completed or at the time of closing.

8.06: Prohibited Practices

(1) It is an unfair or deceptive act or practice for a mortgage broker or lender to make any representation or statement of fact if the representation or statement is false or misleading or has the tendency or capacity to be misleading, or if the mortgage broker or lender does not have sufficient information upon which a reasonable belief in the truth of the representation or statement could be based. Such claims or representations include, but are not limited to the availability, terms, conditions, or charges, incident to the mortgage transaction and the possibility of refinancing. In addition, other such claims and representations by the broker may include the amount of the brokerage fee, the services which will be provided or performed for the brokerage fee, the borrower's right to cancel any agreement with the mortgage broker, the

borrower's right to a refund of the brokerage fee, and the identity of the mortgage lender that will provide the mortgage loan or commitment.

(2) It is an unfair or deceptive act or practice for a broker or lender to charge an application and/or broker fee which significantly deviates from industry-wide standards or is otherwise unconscionable.

(3) It is an unfair or deceptive act or practice for a mortgage broker or lender to accept any broker fee, application fee or other fee, prior to the borrower's receipt of the applicable disclosure forms mandated by 940 CMR 8.05(1), (2) or (3). Notwithstanding the foregoing, an appraisal fee may be accepted if the lender or brokers provides oral or written notice, prior to the receipt of such fee, as to whether the fee is refundable.

(4) It is an unfair or deceptive act or practice for a mortgage broker or lender to engage the services of (another) mortgage broker that will charge the borrower an additional fee without obtaining in advance the written permission of the borrower to charge that fee, the amount of which shall be specified in writing.

(5) It is an unfair or deceptive act or practice for a mortgage broker or lender to directly or indirectly, regardless of the receipt or the expectation of receipt of compensation from the contractor, to:

(a) provide loan application documents to home improvement contractors for use by such contractor in connection with the financing by mortgage loans of home improvement contracts;

(b) use a home improvement contractor as an agent for its business; or

(c) accept mortgage applications from contractors.

This provision shall not prohibit contractors from referring consumers to mortgage brokers or lenders, or lenders from purchasing executed home improvement contracts.

(6) It is an unfair or deceptive act or practice for a mortgage broker or lender to procure or negotiate for a borrower a mortgage loan with rates or other terms which significantly deviate from industry-wide standards or which are otherwise unconscionable. To determine whether the Annual Percentage Rate ("APR"), for example, is unconscionable, factors to consider include whether the APR at the time the loan was made is more than, the greater of:

(a) ten percent above the highest domestic "Prime Rate" listed in the Money Rates section of The Wall Street Journal; or

(b) twenty percent; and

whether the APR is consistent with comparable rates for borrowers in similar financial circumstances.

(7) It is an unfair or deceptive act or practice for a mortgage lender to act also as a mortgage broker directly or indirectly in the same mortgage loan transaction, or to violate 209 CMR 42.04(4) or 42.07(4).

(8) It is an unfair or deceptive act or practice for a lender to fail to disburse funds in accordance with any commitment or agreement with the borrower.

(9) It is an unfair or deceptive act or practice for a mortgage broker or lender to conduct business with a person which should be licensed under M.G.L. c. 255E, and which it knows or should know is an unlicensed mortgage broker or lender.

(10) It is an unfair or deceptive act or practice for any mortgage lender to charge a prepayment fee which:

(a) violates M.G.L. c. 183, § 56;

(b) significantly deviates from industry-wide standards; or

(c) is otherwise unconscionable.

(11) It is an unfair or deceptive act or practice for a mortgage broker or lender to fail to give to the borrower or his or her attorney the time and reasonable opportunity to review every document signed by the borrower and every document which is required pursuant to these regulations, and other applicable laws, rules or regulations, prior to the disbursement of the mortgage funds.

(12) It is an unfair or deceptive act or practice for a mortgage broker or lender to accept any fees which were not disclosed in accordance with these regulations or applicable law.

(13) It is an unfair or deceptive act or practice for a mortgage broker or lender to accept any attorneys' fees in excess of the fees that have been or will be remitted to its attorneys.

(14) It is an unfair or deceptive act or practice for a mortgage broker or lender to refuse to permit the borrower to be represented by the attorney of his or her choice. Nothing contained herein shall limit the lender's right to choose its own attorney, which shall be paid for by the borrower.

(15) It is an unfair or deceptive act or practice for a mortgage broker to arrange or mortgage lender to make a mortgage loan unless the mortgage broker or lender, based on information known at the time the loan is made, reasonably believes at the time the loan is expected to be made that the borrower will be able to repay the loan based upon a consideration of the borrower's income, assets, obligations, employment status, credit history, and financial resources, not limited to the borrower's equity in the dwelling which secures repayment of the loan. The determination under this section of a borrower's ability to repay a loan shall take into account, without limitation: i) the borrower's ability to repay at the fully indexed rate, assuming a fully amortizing repayment schedule, and the resulting scheduled payments that may be

charged under the loan accounting for interest rates, financial terms or scheduled payments that may adjust upward; and ii) the property taxes that are required on the subject property at the time the loan is expected to be made and the reasonably anticipated insurance costs if the loan requires that insurance be maintained on the property, regardless whether the broker or lender will collect an escrow for such taxes or insurance in connection with loan payments. For purposes of this subsection, the "fully indexed rate," with respect to loan rates that may adjust upward, shall mean the index rate prevailing at the date of loan origination plus the margin to be added to it after the expiration of an introductory interest rate. For purposes of illustration, assume that a loan with an initial fixed rate of 7% will reset to the six-month London Interbank Offered Rate (LIBOR) plus a margin of 6%. If the six-month LIBOR rate equals 5.5% at the date of origination, the determination of ability to pay under this subsection shall take into account the borrower's ability to repay at 11.5% (5.5% plus 6%), regardless of any interest rate caps that limit how quickly the fully indexed rate may be reached.

(16) It is an unfair or deceptive act or practice for a mortgage broker or lender to process or make a mortgage loan without documentation to verify the borrower's income (a so-called "no documentation," "no doc," "stated income" or "limited documentation" loan) unless the broker or lender, as applicable, first provides a written document to the borrower, which must be signed by the borrower in advance of the closing, and which: a) identifies the borrower's income and the source of the income; and b) provides detailed information, if true, that by applying for a mortgage loan on a no- or limited documentation basis, the consumer will pay a higher interest rate or increased charges, or have less favorable terms for the mortgage loan (including information concerning the precise increase in interest rate, charges, or the nature of the less favorable terms). Provided, however, that if a mortgage broker or lender arranges or makes a mortgage loan using a No Income Loan Product (as defined herein), which loans shall remain subject to Section 8.06(15), the requirement in clause (a) of the preceding sentence shall not apply. It is an unfair or deceptive act or practice for a mortgage lender or broker to process or make a mortgage loan on a no- or limited documentation basis if the stated income provided by the borrower with respect to the no- or limited documentation loan contradicts information previously obtained by the broker or lender with respect to that borrower in connection with the same proposed loan, absent a documented change in circumstances or other documented explanation for the discrepancy between the prior information and latter income representation. Notwithstanding the foregoing, it shall be an unfair or deceptive act or practice for a mortgage lender to underwrite or close a loan without first verifying the employment or income of the borrower when the amount of the income stated is not reasonable for the actual employment status or experience of the borrower known to the lender, or when the borrower's stated employment or stated income is not reasonable in light of the borrower's circumstances known to the lender.

(17) It is an unfair or deceptive act or practice for a mortgage broker to process, make or arrange a loan that is not in the borrower's interest. Where the financial interest of a mortgage broker conflicts with the interests of the borrower (for example, where the broker's compensation will increase directly or indirectly if the borrower obtains a loan with higher interest rates, increased charges or less favorable terms than those for which a borrower would otherwise qualify), the broker shall disclose the conflict and shall not proceed to process, make or arrange the loan so long as such a conflict exists. It is an unfair or deceptive act or practice for a mortgage broker to

disclaim the duty established by this subsection (17) in a written contract or to assert in oral representations that a broker does not have such a duty in communications with the borrower.

(18) It is an unfair or deceptive act or practice for a mortgage lender (a) to use a pricing model for its mortgage loans which treats borrowers with similar credit criteria and bona fide qualification criteria differently; or (b) to make a mortgage loan when any or all of the cost features of the mortgage loan are based on criteria other than the borrower's credit and other bona fide qualification criteria. For purposes of this paragraph, "bona fide qualification criteria" shall mean those criteria that a lender, pursuant to written loan underwriting or origination policies, takes into account in determining whether to extend a mortgage loan, including by way of example, income, assets, credit history, credit score, income-to-debt ratios or loan-to-value ratios. For purposes of sub-paragraph (b), the term "cost features" shall include, but not be limited to, the interest rate; the index; margin; and other adjustment features if the interest rate is adjustable; points; and prepayment penalties.

8.07: Severability

If any provision of these regulations or the application of such provision to any person or circumstances is held to be invalid, the validity of the remainder of these regulations and the applicability of such provision to other persons or circumstances shall not be affected.

8.08: Effective Date

The amendments to 940 CMR 8.00 shall be effective on January 2, 2008.

OFFICE OF THE ATTORNEY GENERAL
GUIDANCE WITH RESPECT TO 940 CMR 8.00 *et. seq.* (as amended)

On October 17, 2007 the Office of the Attorney General amended 940 CMR 8.00 *et. seq.*, the regulation under the Consumer Protection Act that identifies unfair and deceptive acts or practices in connection with mortgage brokering and mortgage lending. The new amended regulations were issued following an extensive comment period and after four hearings were held statewide between September 18 and 21, 2007. The new regulations will take effect on January 2, 2008.

Since the regulations were promulgated, the Office of the Attorney General has received inquiries concerning the scope of certain regulations and questions relating to implementation of the regulations. The Office of the Attorney General has changed certain parts of the regulation, first by extending the effective date (which occurred in November); second, by changing Section 8.05 which requires certain disclosures to be provided to consumers; and third, by revising Section 8.06(16) to account for so-called "No Income" products. Also, in order to provide clarity on the issues raised in communications with the Office of the Attorney General, and to assist in the implementation of the regulations, the Office of the Attorney General issues this guidance.

Effective Date

Q. When are the new regulations effective?

All the revised regulations are effective January 2, 2008. When the regulations were first announced, certain parts were effective January 2, 2008, while most parts were effective November 15, 2007. On November 12, 2007, the Attorney General announced that all of the regulations would be effective January 2, 2008, in order to provide industry participants additional time to understand, and prepare implementation of, the new regulations. All regulations are effective January 2, 2008.

Q. Do the regulations affect mortgage loans that are "in the pipeline" prior to January 2, 2008 but have not closed by the effective date?

No. In order to provide certainty to lenders and brokers and in order to prevent disrupting loan transactions that were planned in 2007 but still await consummation or "closing," the regulations will apply only to loan applications received on or after January 2, 2008. If a borrower provides a complete loan application to a broker or lender in advance of January 2, 2008, then these regulations will not apply to that prospective loan.

Changes in the Regulations Since their Announcement in October

Q. What has changed since these regulations were first announced on October 17, 2007?

Three things have changed since these regulations were first announced on October 17. First, the effective date changed. The effective date initially was November 15, 2007 for most of the regulations. In November, the Attorney General changed the effective date to January 2, 2008 for all regulations. Second, the office of the Attorney General changed the originally announced regulation by revising Section 8.05 governing disclosures to borrowers. The original revised regulation required two disclosure forms—one for brokers and one for lenders—that were required to be provided to borrowers. As of the filing of the final regulation, those new forms are no longer required. Instead, Section 8.05 provides that it is unfair or deceptive for a lender or broker to fail to provide to a borrower a disclosure required by federal or state law. Third, Section 8.06(16), which restricts the use of so-called "stated income" products, has been revised to account for so-called "No Income" loan products. These products—where a lender in no way considers employment status or income because the lender's decision is based on other criteria—no longer require a borrower's signed statement of income. *See* Sections 8.03 (definition of "No Income Loan Product") and 8.06(16).

Scope of Regulations

Q. Do these regulations apply only to "subprime" mortgage loans?

Sections 8.02 and 8.03 exempt reverse mortgages and open-end home equity lines of credit from these regulations, as well as reduced interest rate mortgage originated under governmental affordable housing programs. *See* Sections 8.02 (Scope) and 8.03 (definition of mortgage loan). Beyond those exemptions, the regulations apply to all residential mortgage loans, not any particular subset of loans. The application of the regulations is not limited to loans known as "subprime," high cost, or nonconventional loans.

Q. Are banks or depository institutions excluded from the regulations?

No. Banks and depository institutions are not exempt from the regulations. Banks and depository institutions, presuming they make residential mortgage loans, are "mortgage lenders" under the regulations.

Q. Do the regulations apply to commercial loans or only residential mortgage loans?

The regulations apply only to residential mortgage loans, not to commercial loans. The definitions for "mortgage broker," "mortgage lender," "mortgage loan," and "residential property" in the regulations all reflect the application of the regulations to residential mortgage loans.

Assessment of Reasonable Ability to Pay (Section 8.06(15)

Q. Under subsection 8.06(15), may a lender or broker qualify a borrower for an adjustable rate mortgage with a fixed starter rate based on the borrower's ability to repay only at the fixed starter rate?

No, the lender or broker must also take into account the loan rates and terms that adjust following the fixed rate period. Section 8.06(15) requires that lenders or brokers must reasonably determine the borrower's ability to repay the loan. That determination must *take into account* the borrower's ability to pay at the fully-indexed rate. If the duration of the fixed starter rate is relatively short (such as 2 or 3 years for 2/28 or 3/27 ARM loans), then in order to comply with Section 8.06(15) the lender certainly should determine the borrower's ability to pay the monthly payments at the fully indexed rate, following the ARM adjustment. If the duration of the fixed starter rate is considerably longer (such as 5, 7 or 10 years), then the lender has increased flexibility in *taking into account* the fully indexed rate in reasonably assessing the borrower's ability to repay. (See further discussion immediately below).

Q. Does this regulation mean that the borrower must be qualified for the loan based on the ability to pay at the interest rate that adjusts upward in the future, even if the initial interest rate is fixed (and the adjustment does not occur) for five, seven or ten years?

The overarching principle set forth in Section 8.06(15), set forth in the first sentence, is that lenders and brokers, based on information known at the time the loan is made, must "reasonably believe" that "the borrower will be able to repay the loan." The second sentence then requires that the determination of a borrower's ability to repay "shall take into account, without limitation, . . . the borrower's ability to repay at the fully indexed rate . . . ." Therefore, lenders and brokers must *take into account* upward adjusting terms and their impact on scheduled payments. Accordingly, with respect to a two year fixed/twenty-eight year adjustable loan, a lender could not qualify a borrower based on the two year introductory terms alone, without taking into account the predictable increase in payments two years after loan origination. Likewise with an ARM loan that features a much longer fixed rate period (for instance, five, seven or as long as ten years), the lender still must *take into account* the future increase in interest rate and its impact on monthly payments. The regulation does not dictate precisely how lenders and brokers must underwrite ARM loans to account for those upward adjustments. But the regulation plainly prohibits lenders and brokers from *ignoring* those upward adjustments and increased payments—qualifying borrowers based only on a short term, low interest rate and artificially low monthly payment.

In determining *how* to take into account increased rates, changed terms or increased payments following an ARM adjustment, it is expected that lenders and brokers would reasonably take into account, for example: i) the duration of the introductory, fixed rate period; ii) the magnitude of the ARM adjustment when it occurs; iii) subsequent ARM adjustments, accounting for caps applicable to periodic adjustments as well as overall

caps; iv) the resulting impact on the borrower's expected monthly payment obligation; and v) other underwriting criteria used by the lender to reasonably determine whether the borrower will be able to repay the loan both during the introductory period and after the ARM adjustments.

Q. Does this regulation require all lenders to collect an escrow for property tax or insurance payments?

No. This regulation does not mandate that lenders collect property tax or insurance escrows. The regulation does require that lenders, when determining a borrower's ability to repay, must take into account property taxes and insurance based on tax and insurance costs on the property at the time of the loan, regardless of whether the lender collects them.

Restrictions on Stated Income or No-Doc Loans (Section 8.06(16))

Q. Does subsection 8.06(16) ban the use of "no–doc" or "stated income" loans?

No, those loan products may still be offered and used. In order to curtail abuse of these products, this subsection requires lenders to obtain a signed statement from the borrower stating borrower's income, even though a lender may choose not to verify or document the income so stated by the borrower. The signed statement also must disclose the impact of the no- or low-documentation feature on the loan terms and costs.

Q. Are there exemptions from this part of the regulation? For instance, for loans with low loan-to-value ratios, or where an existing borrower is obtaining a refinancing to decrease the interest rate or to improve other terms?

Section 8.06(16) provides one exception from part of the regulation, for "No Income Loan Products." A "No Income Loan Product" is one where the lender, pursuant to its written underwriting or origination policy, in no way considers a borrower's income or employment status. If a broker arranges or a lender makes a loan using a No Income Loan Product, then he or she need not collect a signed statement of the borrower's income as required by clause (a) of Section 8.06(16). The broker or lender still must disclose how the No Income Loan Product increases the applicable interest rate or other costs, if that is the case.

Beyond that exception, Section 8.06(16) does not include exemptions for certain loans or borrower characteristics. For any loan where the broker or lender considers income but does not require documentation to verify the borrower's income, the broker or lender must have the borrower sign a document that (i) identifies income and source of income and (ii) discloses the impact of the low-documentation or no-documentation loan product on the loan terms.

Q. Has the Office of the Attorney General issued a form to comply with Section 8.06(16)?

No. The regulation does not specify or require a particular form.

Mortgage Broker Conflicts of Interest and Mortgage Broker Compensation (Section 8.06(17))

Q. Does Section 8.06(17) of the regulation ban all Yield Spread Premiums, or YSP's?

No, Section 8.06(17) does not ban all Yield Spread Premiums ("YSP's"). It bans only those kind of YSP's, and other forms of broker compensation, that place the broker's financial interest into conflict with the interests of the broker's client.

Section 8.06(17) sets forth two principles, both of which serve to prohibit an unfair conflict between the broker's interests and those of the borrower/client. First, it is unfair or deceptive "for a mortgage broker to process, make or arrange a loan that is not in the borrower's interest." Second, "where the financial interest of a mortgage broker conflicts with the interests of the borrower . . . , the broker shall disclose the conflict and shall not proceed to process, make or arrange the loan so long as such a conflict exists."

This regulation acknowledges, of course, that brokers expect to be paid for their services, in some manner. YSP's, generally speaking, are a form of broker compensation where the lender pays a broker for selling a loan, not through points or other charges paid at the loan closing (and often paid from the loan proceeds), but instead by the lender paying the broker a certain amount, or certain percentage of the loan, outside of closing. The YSP then would permit the lender to recoup over the loan period that compensation paid to the broker. By itself, and with appropriate disclosure, that type of YSP does not raise a conflict between the broker's interests and those of the client. Even though in those circumstances the interest rate on a loan may increase if a broker gets paid a YSP, the alternative to this YSP arrangement typically would have the borrower pay sales costs in the form of fees or a point (or points) at closing. Because both alternatives require the borrower to pay compensation to the broker – directly through a fee at closing or indirectly through a slightly higher interest rate that funds the YSP – this general concept of YSP compensation does not necessarily raise a conflict of interest and therefore is not banned by the regulation, provided that the compensation options are accurately disclosed to borrowers.

In contrast, in a situation where a broker is paid YSP compensation that escalates upward as the loan interest rate increases, with no corresponding benefit to the borrower (such as the benefit of avoiding points or closing costs), that type of YSP generates a conflict between the financial interest of the broker and the borrower's interest. Section 8.06(17) makes such a conflict of interest unfair or deceptive in violation of chapter 93A.

Q. Must YSP's be disclosed to the borrower?

Yes. Section 8.05(2) of the regulations requires lenders and brokers to disclose to borrowers all material facts relating to a transaction. All compensation paid by lenders to brokers, and how that compensation is calculated, are material facts that must be disclosed to borrowers. Further, federal and state laws that require certain borrower disclosures reinforce that YSP's and other broker compensation must be disclosed (for example, the HUD-1 settlement statement requires disclosure of YSP's).

Q. Do these regulations mean that a mortgage broker can no longer arrange a loan with no closing costs/no points, and instead must collect any fees or points directly at the closing?

No. Section 8.06(17) permits a mortgage broker to offer a borrower alternatives with respect to how the mortgage broker's compensation will be paid. For example, if a broker arranges a no closing costs/no points loan, then often the broker will be compensated directly by the lender through a YSP. In that case, as an alternative to paying the closing costs at closing, the borrower's loan would be at a slightly higher interest rate. Often the borrower may be able to obtain a lower interest rate, but would have to pay closing costs. Further, the borrower may even be able to pay cash to reduce their interest rate (for example, "discount points"). It is permissible for a broker to present choices to borrowers, which often reflect options between up-front costs to the borrower versus longer term costs such as an increased interest rate. It is not permissible under this regulation for the financial interest of the broker to conflict with the interest of the borrower.

Q. How can a broker determine when the broker's compensation generates a conflict with the interests of their client, the borrower?

Set forth below is a simple example of some basic compensation options involving a potential combination of YSP's as well as points. Presume, for purposes of this example, that a borrower has chosen to use a broker to obtain a mortgage loan. The borrower qualifies for, and has chosen, a 30 year fixed rate mortgage. Also presume with respect to all the scenarios below, for sake of simplicity, that all lenders with whom the broker places loans have offered the same terms and the same set of compensation options. As reflected in the chart, the borrower qualifies for a 7.0% interest rate if willing to pay 1.5 points at closing, and qualifies for a no-points, no closing costs loan at 7.5%, with the lender paying broker a YSP equal to 1.5 points. There are options in between those, as well as others, reflected in the chart below. Please keep in mind that these figures are for illustrative purposes only. These regulations do not authorize any particular level of compensation to mortgage brokers or originators:

Scenario	Points at closing	Interest Rate	YSP Lender to Broker	
A	**1.5**	**7.00%**	**Zero**	
B	**0.75**	**7.25%**	**.75%**	
C	**Zero**	**7.50%**	**1.5%**	
D	**Zero**	**7.75%**	**2.25%**	**[conflict]**
E	**1.5**	**7.50%**	**1.5%**	**[conflict]**

In each of scenarios A, B and C, there is a benefit to the borrower when the broker is paid by YSP, namely, a reduction in points paid at closing. Further, the broker's compensation, though paid in different ways, is roughly equivalent (1.5 points) in each scenario A, B and C. In contrast, in this example (which presumes that each of these scenarios A through E is available to the borrower), scenario D and E portray a conflict between the broker's compensation and the borrower's interest. In scenario D, the broker increased his compensation .75% on account of the borrower's increased interest rate, with no corresponding benefit to the borrower (as compared to A, B and C). In scenario E, the broker received both points and YSP, increasing his compensation (as compared to A, B and C), ignoring the available option (scenario C) that would have achieved the same interest rate without paying the broker 1.5 points at closing.

Q. Can the Office of the Attorney General provide an example of what YSP's are permissible and what YSP's would violate the regulation?

Following is a simple example to illustrate the discussion in the previous questions concerning Section 8.06(17). The first two options below show borrower choices, including YSP compensation, that would not violate the regulation.

Presume that a borrower needs a loan for $200,000 to purchase a home.

First Option: The broker explains to his client that he can place the client in a 30-year fixed rate loan at 7.50%. Presume that this is the lowest rate for which the borrower qualifies. The broker explains that, to cover broker's costs, that loan will cost one point (or $2,000), to be paid at the closing. The broker further explains that the borrower can either pay that $2,000 in cash or can fold it into the loan, in which case the borrower will then need to borrow $202,000.

Second Option: The broker explains a second option to the borrower. If the borrower would prefer not to pay a point, then the broker can place the borrower in a 30-year fixed rate loan at 7.75%, with no points. The broker further explains that, if you choose this approach, the lender will pay the broker directly $2,000. That amount will not increase

the borrower's loan amount, but of course, the loan will be more expensive because of the higher interest rate (plus .25%).

In this scenario, the broker has presented two compensation alternatives to the borrower and those alternatives do not present a conflict between the broker's financial interest and the borrower's. They are reasonable alternatives for the borrower, and each compensates the broker roughly the same.

Third Option, impermissible because it generates a conflict of interest: Presume again that the borrower needs a $200,000 loan and qualifies for a thirty year fixed rate. The broker offers to place a 7.5% loan with a fee equal to one point ($2,000). The broker offers the alternative of placing a 7.75% loan with no points, where the broker will be compensated $2,000 by the lender, through a YSP. Further, pursuant to a rate sheet provided by the lender, if the broker closes a loan with an interest rate of 8.00% loan, the broker will be paid 2 points by the lender, or $4,000. If the broker offered to place his client in the 8.00% loan, to generate additional compensation from the lender, that recommendation would violate Section 8.06(17). In that scenario, the broker's compensation increased for recommending to his client a more expensive loan. The financial interest of the broker conflicted with his client's interest, and under the regulation it is unfair or deceptive for that transaction to go forward so long as the conflict exists.

Q. If a conflict exists between the broker's financial interest and the borrower's interest, can the loan transaction go forward so long as the conflict is disclosed to the borrower?

No. Under the regulation, if a conflict exists between broker and borrower's interests, the broker must disclose the conflict <u>and</u> "shall not proceed to process, make or arrange the loan so long as a conflict exists."

Q. If a conflict exists, can the loan transaction go forward if the broker gets the borrower to sign a form that acknowledges the conflict and waives any objection?

No. Under the regulation, if a conflict exists between broker and borrower's interests, the broker must disclose the conflict <u>and</u> "shall not proceed to process, make or arrange the loan so long as a conflict exists."

Q. If one broker, generally speaking, charges 1.5 points per loan transaction, whether compensated in points or charges at closing or compensated via a YSP, but another broker in the same locality charges only about 1 point per loan, is the first broker obligated to change his pricing to avoid a conflict of interest because a borrower may be able to pay less by using a competing broker?

No. The conflict of interest analysis is specific to each mortgage broker. The regulation does not require all brokers to charge the same amount, and does not require brokers to match the compensation rates of any competitor.

Q. If a person holds both a mortgage broker license and a mortgage lender license, when does Section 8.06(17) apply and when does section 8.06(18) apply?

In circumstances when a person is acting as a mortgage broker, he or she must comply with subsection 17, and if a person is making a loan as mortgage lender than he or she must comply with subsection 18. It is understood that certain persons hold both lender and broker licenses, and their obligations under the regulations will depend on the capacity in which they operate. Note that, under Section 8.06(7), a person may not receive compensation, in the same transaction, as both a broker and a lender. *See also* Division of Banks regulations, 209 C.M.R. 42.04(4) & 42.07(4) (prohibiting a licensee from serving as both lender and broker in the same transaction).

Anti-Steering Provision for Mortgage Lenders (Section 8.06(18))

Q. Are lenders allowed to offer special pricing or special loan terms for particular categories of borrowers? For instance, can a lender offer a better interest rate, or better loan terms: a) to a borrower that has multiple accounts with a lending bank? b) to a borrower that has a successful payment history on other accounts with the same lender? c) to a borrower that agrees to make monthly payments using an automatic debit feature?

Section 8.06(18) is designed to prohibit a mortgage lender's loan originators from steering borrowers to higher cost loans and to prohibit price gouging, that is, charging increased costs and fees that bear no relation to the borrower's qualifications or the credit risk posed by borrower. The regulation achieves this by requiring that a lender's pricing model, and the costs features of a loan, must be based on a borrower's credit criteria and "bona fide qualification criteria."

The regulation does not, however, dictate the "bona fide qualification criteria" that lenders may consider in underwriting and pricing a loan. Instead, bona fide qualification criteria "shall mean those criteria that a lender, pursuant to written loan underwriting or origination policies, takes into account in determining whether to extend a mortgage loan." This requires that the criteria be reflected in the lender's written policies, but does not dictate the criteria that may be considered. Of course, a lender cannot use criteria that discriminate based on race, ethnicity or other criteria prohibited by law. This regulation, however, extends beyond unlawful discrimination to prohibit steering borrowers to higher cost products based on factors other than "bona fide qualification criteria."

Therefore, each of the examples referenced above would be permissible so long as the lender has made a determination, reflected in its underwriting or origination policies, to

consistently take those criteria into account. It makes sense that a lender, in deciding whether to extend credit and on what terms, would take into account things like multiple accounts, or the lender's prior credit history with the borrower. Likewise, it makes sense that a lender would positively view a borrower's automatic payment agreement in its determination whether to extend credit and on what terms. So long as lenders apply their bona fide qualification criteria consistently, they would not violate Section 8.06(18).

Q. Under Section 8.06(18), can a borrower pay a discount point to reduce the loan's interest rate, without violating the requirement that pricing models and cost features be based on credit or bona fide qualification criteria?

Yes. So long as the same set of loan options and costs features—including in this example the ability to pay money to buy-down the borrower's interest rate—are made available to all borrowers with similar qualifications, this regulation does not ban those options.

Q. Does Section 8.06(18) prevent a lender from carrying out its goals under the Community Reinvestment Act or other programs designed to target lending to communities or borrowers that are in need?

No. A lender's institutional goals under the CRA or similar programs presumably would be reflected in the lender's underwriting or origination policies and, therefore, may be taken into account in determining whether to make loans and on what terms.

Q. Does Section 8.06(18) limit the flexibility of mortgage lenders or community banks to offer special or favorable terms to borrowers? For instance, if a homeowner currently has a subprime loan and faces potential default and the homeowner would not qualify for a conventional loan, can a lender offer special terms to help the borrower refinance? Or if a local teacher has difficulty affording payments on a conventional loan, can a lender offer special terms to help make housing affordable??

The new regulations do not prohibit lenders from addressing the unique needs of different borrowers, including needs to refinance subprime loans. Section 8.06(18) is designed to ban lender price-gouging, steering into higher cost products, and impermissible discrimination, while maintaining a lender's flexibility to establish its own "qualification criteria." The regulation requires that a lender's bona fide qualification criteria be reflected in a written underwriting or loan origination policy. However, the regulation does not dictate a lender's bona fide qualification criteria. Accordingly, lenders may consider a variety of reasonable qualification criteria (so long as not otherwise prohibited by law, such as race or ethnicity). Thus, a community-based lender could reasonably determine that its underwriting or loan origination policies will take into account, for instance, a policy to encourage home ownership for first-time homebuyers, or a policy to assist teachers or firefighters to live in the community where they work. Similarly, a lender could have an underwriting or loan origination policy that reflected a policy to preserve home ownership by extending certain favorable terms to borrowers

who need relief (*e.g.*, refinancing) from unaffordable, predatory loans. Those types of reasonable and beneficial lending policies are not prohibited by this regulation. Indeed, the Office of the Attorney General encourages that type of lender flexibility which will be necessary to preserve home ownership for borrowers facing unaffordable loans. This regulation preserves lender flexibility, but prevents abusive practices like steering and discrimination.

Q. Does Section 8.06(18) prohibit lenders from "meeting the competition" to make a loan? For instance, if a potential borrower provides a quote from a competitor at a ¼ point lower interest rate, can a lender reduce its rate to try to meet the competition and win the customer's business?

Section 8.06(18) does not stop lenders from competing with each other to win the business of borrowers. As a threshold matter, the Consumer Protection Act is designed to protect consumers as well as to promote fair competition. The statute, and these regulations under the statute, must be interpreted consistent with that statutory purpose. Accordingly, the regulations should not be interpreted in a manner to discourage competition, including price competition.

Section 8.06(18) *does* prohibit unbridled discretionary pricing of loan products, by requiring that a lender's pricing model and loan cost features be based on a borrower's qualification criteria. The regulation thus prevents loan originators from steering borrowers to higher cost loans or charging increased costs and fees that bear no relation to the borrower's qualifications or the credit risk posed by borrower. The regulation does not dictate the "qualification criteria" that may be considered by a lender, although it does require that those criteria be reflected in a written loan underwriting or origination policy. A lender could reasonably choose to include, among the qualification criteria it considers in its loan origination policy, the need to meet a competitive quote in order to win a customer's business. If that permissible flexibility were misused—for instance, as a justification for price gouging or discrimination—then such misconduct would not comply with the regulation; the purported qualification criteria would not be *bona fide*. So long as this flexibility is not used as a subterfuge for prohibited conduct, Section 8.06(18) allows lenders to meet the competition as part of their loan origination policies.

Disclosure Forms (Section 8.05)

Q. Why did the Attorney General change the disclosure regulation in Section 8.05 from the version announced on October 17, 2007?

Several reasons. First, one focus of the Attorney General disclosure form was to require lenders and brokers to prominently disclose to borrowers the impact on monthly payments of interest rate adjustments that occur with adjustable rate mortgage ("ARM") loans, sometimes referred to as the "payment shock" of ARM loans. In November 2007, Governor Deval Patrick signed legislation that addresses issues surrounding nonconventional mortgage products including ARM loans particularly. Under the new law, a borrower may not be placed into a nonconventional ARM loan unless they

affirmatively opt in to that product, and then only after completing counseling by a certified counseling agency. That law significantly changes the process of buying ARM loans for Massachusetts borrowers, causing the Attorney General's office to reevaluate the disclosure aimed substantially at the same risks posed by ARM loans. Second, the office has heard in recent weeks and months from numerous stakeholders that questioned the utility and value of a new disclosure form, which would be added to a number of other borrower disclosure forms already required by federal and state law. Given the number of existing required disclosures and in order to avoid adding duplicative or inefficient requirements the already paper-intensive mortgage loan process, the Attorney General determined it was best to reconsider adding new required disclosures and instead will work to impact existing disclosure requirements, by working with the Division of Banks and other regulators to ensure consumers get the information they need concerning their mortgage loan.

Q. Does this new Section 8.05 supersede the old Section 8.05, which required form disclosures for certain home equity loans?

Yes. The amended Section 8.05 supersedes the prior version, which required that certain forms be used. The prior Attorney General disclosure forms, which pertained to certain types of mortgage loans, are no longer required. Instead of requiring an additional disclosure form, this regulation simply requires compliance with other disclosure requirements in state and federal law.

Q. Does this regulation demand that a lender or broker translate disclosures into all possible languages, regardless of costs? And must a lender or broker provide an adult interpreter for all languages, regardless of costs?

No. Section 8.05(3) requires that lenders and brokers "take reasonable steps to communicate the material facts of [loan] transactions in a language that is understood by the borrower." The regulation then provides a "safe harbor," that is, ways that a lender or broker can assure compliance with the "reasonable steps" requirement. That safe harbor provides that "reasonable steps *which shall comply with this regulation* may include but shall not be limited to: a) using adult interpreters; and b) providing the borrower with a translated copy of [disclosure forms]." Those steps thus are not required, but would comply with the regulation if taken.

Relation to Other Laws

Q. How do these regulations change the law? Is this the first time chapter 93A has been applied to mortgage lenders and mortgage brokers?

In a general sense, these regulations do not change the law. The Consumer Protection Act , chapter 93A, has long applied to mortgage brokers and lenders. In the absence of these regulations, it is still unlawful for mortgage lenders or brokers to engage in unfair or deceptive acts or practices—to mislead borrowers, to fail to disclose material facts such as how brokers are compensated, or to make loans with unconscionable terms. The

Attorney General, prior to promulgating these regulations, has brought enforcement actions alleging, for instance, that it is unfair or deceptive for a lender or broker to fail to reasonably assess a borrower's ability to pay (an issue now addressed by Section 8.06(15)) or for brokers or lenders to steer borrowers to more expensive products in order to increase broker or loan officer compensation (an issue now addressed by Sections 8.06 (17) and (18)). Indeed, each of the standards of conduct set forth in the regulations can be traced to the Office of the Attorney General's experience in investigating and litigating chapter 93A enforcement actions against brokers or lenders. Accordingly, in that manner these regulations do not change the existing law. In addition to authorizing Attorney General enforcement actions, however, the Consumer Protection Act authorizes the Attorney General to issue regulations that identify specific conduct as unfair or deceptive. That is what these new regulations do in the business of selling residential mortgage loans. Once unfair or deceptive conduct is identified by an Attorney General regulation, a violation of the regulation comprises an unfair or deceptive act or practice in violation of chapter 93A. The regulations provide more precise standards for fair and nondeceptive lending practices.

Q. Are these regulations related to the Massachusetts law passed in November 2007 that contains new provisions related to certain mortgage loans, mortgage originators and foreclosure protection?

These regulations are issued by the Attorney General under the Consumer Protection Act, chapter 93A. They are not promulgated pursuant to any other law, including a law recently passed by the Massachusetts Legislature. That law provides new protections for homeowners facing foreclosure, including a 90 day right to cure, requires broader licensing of mortgage originators, and places restrictions on the sale of nonconventional adjustable rate mortgage loans, among other things. The provisions of the Attorney General's regulations are not present in the recent Massachusetts statute. The regulations thus complement the new law.

Q. Why is the Attorney General implementing these regulations now, when federal regulators also are considering new standards to protect consumers who purchase mortgage loans?

The Office of the Attorney General determined, based on its experience investigating and litigating unfair and deceptive lending practices, and based on the public hearings preceding these regulations, that certain unfair and deceptive conduct was sufficiently widespread that it demanded to be addressed by regulations in order to ensure that the misconduct is not repeated in the future. In recent months, other regulators also have sought to address similar issues. However, the new Massachusetts law does not include the standards set forth in these regulations. Likewise, the U.S. House of Representatives passed a bill, but that measure has not passed the Senate. Also, federal banking regulators have announced an intention to issue *proposed* regulations that may address certain unfair or deceptive lending conduct, but those proposed regulations may take months or years to be finalized and effective. In light of the scale of recent lending misconduct observed by the Office of the Attorney General, the Attorney General is

unwilling to wait for others to issue standards of lending fairness to protect Massachusetts consumers. However, if state or federal regulators enact new laws that touch on the mortgage broker and lender standards set forth in 940 C.M.R. Part 8, the Office of the Attorney General will promptly analyze those new laws to ensure consistency and avoid having in place regulations that are duplicative or unnecessary.