8 Hour GA SAFE Comprehensive: Compliance for 2024

ProEducate
4200 S. I-10 Service Rd., W.
Suite 134
Metairie, LA 70001

Date of Course Content: 6/01/24
Date of Course Approval:

Provider ID: 140003

 ©All Rights Reserved

Module 1 Federal Laws

In the following sections, "CFR" stands for "Code of Federal Regulations" and "USC" stands for "United States Code". Once Congress passes a law it is recorded in the United States Code (USC) books. The Code of Federal Regulations (CFR) are regulations issued by the various agencies which congress assigned to enforce the various laws (code) it adopted. The agencies explain their interpretation of those laws assigned to them and how it intends to implement it.

Other abbreviations include:

"MMC" – Multi-State Mortgage Committee

"CSBS" – Conference of State Bank Supervisors

"AARMR" – American Association of Residential Mortgage Regulators

"CFPB" – Consumer Financial Protection Bureau

"MME" – Multi-State Mortgage Entities

"NMLS" – Nationwide Mortgage Licensing System

"SAFE Act" - Secure and Fair Enforcement for Mortgage Licensing Act

Federal Laws Course Objective

This lesson will provide the student with an understanding of the most common issues found with MMC examinations. The course discusses the purpose of the MMC examination, and the required topics for the most repeated or outrageous non-compliance violations discovered during examinations. Students will review the examination deficiencies and the regulations to understand how to properly comply with the regulations. The federal law sections covered include ECOA appraisal timing, FCRA & ECOA adverse action letters, TILA Right to Rescission, TILA loan fee tolerance, and TILA timing requirements.

Multi-state Mortgage Committee

Mortgage lenders that have multiple locations in several states face challenges to ensure their company's originations meet all federal and state law regulations. In the past, large lenders, termed Multi-state Mortgage Entities (MMEs), struggled as some of their procedures would meet the regulations in one state only to have different state find fault with their compliance. Some federal agencies that oversaw mortgage laws would also conflict on what was considered regulation

 ©All Rights Reserved

compliance. MME compliance was near impossible which left many putting complete compliance as a low priority, and managed as best they could and paid the fines when they came.

With the passing of the Dodd Frank Wallstreet Reform and Consumer Protection Act (Dodd-Frank Act), the industry was given structure, and path to uniform compliance on a national level, along with a watch dog compliance enforcer. The Consumer Finance Protection Bureau was established to provide uniform interpretation and compliance enforcement of federal mortgage lending regulations. The Consumer Financial Protection Bureau (CFPB) was given authority to examine loan files of state licensees and monitor consumer complaints regarding proposed violations. When the CFPB receives a sufficient number of complaints, it has the authority to further investigate the issue, however its main focus is on multi-state large, licensed entities (MMEs).

To assist CFPB in overseeing multi-state compliance for MMEs, a Multi-State Mortgage Committee (MMC) was established. The Committee is comprised of ten appointed State Regulator members and one Conference of State Bank Supervisors (CSBS) member. Their role is to implement cooperative protocols between state agencies and the mortgage industry. The committee issued a CSBS-AARMR MMC Exam Manual to provide guidance for compliance. [1]

With the invaluable information found in examining these large MMEs, NMLS is provided with the compliance topics to cover for annual licensee education requirements. This allows the mortgage industry to self-correct potential inaccurate handling of federal law compliance. The examinations of the MMEs provide guidance for CFPB to understand the problem compliance areas. To improve these deficits, the MMC provides examination reports quarterly that outline the current compliance issues identified by the examinations. This course covers the required CE topics for 2024 ranked by the Multi-State Mortgage Committee (MMC) and was derived from the 2021 third quarter examination reports.

Licensees complying with the regulations save money and time in state examinations. Violations found during examinations may require written letters of explanation, corrective action plans, refunds, and assessed penalties. Examination fees are paid by the licensee under examination and can be expensive when non-compliance is identified or suspected.

[1] https://www.csbs.org/system/files/2019-05/MMC%20Mortgage%20Examination%20Manual%20v2%20-%20May%202019.pdf

 ©All Rights Reserved

State Regulator

The state regulators manage the licensing and supervising of state-chartered banks and non-bank entities that include mortgage lenders, mortgage bankers, and mortgage brokers. It is their responsibility to ensure licensees in their state comply with all regulations and operate their business in a safe and sound manner so as to help their communities. The CFPB may also examine non-bank entities as a joint effort with state regulators.

State Regulators during their examination determine if the non-bank entity is operating in compliance, properly educating their employees, and are properly licensed for the lending provided. The examination will include a review of the financial institutions' loans and corporate records to decide whether the entities are effectively meeting the requirement to operate, monitor, and control risks associated with loan origination activities. Proper record retention is important to prove compliance.

Mortgage Loan Originators

An Individual Mortgage Loan Originator (MLO) may be held accountable by State Regulators for violations found during examinations. It is then their responsibility to comply with the regulations, and pay any fines, penalties, or hearing expense required.

MLOs that lead a team need to be sure their unlicensed assistants are not using their license number to handle licensed activities on their behalf. Their actions may cause a licensee to lose their license and livelihood. It is not the unlicensed person's career they are ruining.

Federal Law Compliance Matters

ECOA Adverse Action Compliance

"Unknown Reason" for Loan Denial

The MMC examinations of the top MMEs found the need to give out Citations for violations of ECOA by stating "Unknown Reason" and not providing the principal reason for denying an application. The ECOA Notice of Adverse Action is required to satisfy the disclosure requirements for ECOA and FCRA and includes a statement of specific reason for the credit denial.[2]

---

[2] 12 CFR § 1002.9(b)(2)-9

©All Rights Reserved

In the official interpretation of Regulation B, the Equal Credit Opportunity Act (ECOA) requires disclosure of the principal reasons for denying or taking adverse action on an application for an extension of credit. The lender is encouraged to provide all reasons used to deny the credit request.

ECOA prohibits creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided they have the capacity to enter a binding contract), receipt of public assistance income, or because the applicant exercised in good faith any Consumer Credit Protection Act.

In addition, the Fair Credit Reporting Act (FCRA) requires a creditor to disclose when it has based its decision in whole or in part on information from a source other than the applicant or its own files. Disclosing that a credit report was obtained and used in the denial of the application, as the FCRA requires, does not satisfy the ECOA requirement to disclose specific reasons for denial.

FCRA example - If the applicant's credit history reveals delinquent credit obligations and the application is denied for that reason, to satisfy the regulation the creditor must disclose the application was denied because of the applicant's delinquent credit obligations.[3] This notice of the credit reports use will accompany how the consumer may obtain a free copy of the credit report used to deny their credit request.

A consumer should be allowed to know the reason they were denied credit. The statement of reasons for adverse action required must be specific and indicate the principal reason(s) for the adverse action. Statements that the adverse action was based on the creditor's internal standards or policies or that the applicant, joint applicant, or similar party failed to achieve a qualifying score on the creditor's credit scoring system are insufficient. The regulation does not mandate that a specific number of reasons be disclosed, but disclosure of more than four reasons is not likely to be helpful to the applicant.

ECOA example – If the consumer receives an adverse action notice with a statement of denial, due to the credit being unable to verify his employment and no other reason is provided, the average consumer may assume he would have gotten approved if his employment were verified. A reasonable

[3] ECOA - 12 C.F.R. §1002.9(b)(2-9)

 ©All Rights Reserved

assumption for a consumer might be that if he is able to provide the verification, he should be approved for the requested loan.

To be accurate, the statement of denial should have included all applicable reasons for denial, such as unable to verify qualifying income, income unstable, and debt to income ratio exceeds allowable threshold for the loan program. This statement provides the consumer direction on the issues he will need to overcome to be creditworthy. These statement of reason in the adverse action letter require the information to the consumer to be clear and concise.

The specific reasons disclosed must relate to and accurately describe the factors actually considered or scored by a creditor. A creditor need not describe how or why a factor adversely affected an applicant.

ECOA example - the notice may say "length of residence" rather than "too short a period of residence."

If a creditor bases the denial or other adverse action on a credit scoring system, the reasons disclosed must relate only to those factors actually scored in the system. Moreover, no factor that was a principal reason for adverse action may be excluded from the disclosure. The creditor must disclose the actual reasons for denial even if the relationship of that factor to predicting creditworthiness may not be clear to the applicant.

For example - "credit score too low," yet how high does it need to be is not provided.

FCRA regulation does not require that any one method be used for selecting reasons for a credit denial or other adverse action that is based on a credit scoring system. Various methods will meet the requirements of the regulation.

1. One method is to identify the factors for which the applicant's score fell below the average score for each factor achieved by the applicants whose total score was at or slightly above the minimum passing score.
2. Another method is to identify the factors for which the applicant's score fell furthest below the average score for each of those factors achieved by all applicants. These average scores could be calculated during the development or use of the system.
3. Any other method that produces results substantially similar to either of these methods is also acceptable under the regulation.

 ©All Rights Reserved

However, if a creditor uses a judgmental system (manual underwrite), the reasons for the denial or other adverse action must relate to those factors in the applicant's record reviewed by the person making the decision.

Combined Credit Scoring and Judgmental System

An underwriter for a mortgage lender makes a credit decision after they review many factors. This is termed a judgmental system. If a creditor denies an application based on a credit evaluation system that employs both credit scoring and judgmental components, the reasons for the denial must come from the component of the system that the applicant failed.

For example - If a creditor initially credit scores an application and denies the credit request as a result of that scoring, the reasons disclosed to the applicant must relate to the credit factors that scored in the system.

If the application passes the credit scoring stage but the creditor then denies the credit request based on a judgmental assessment of the applicant's record, the reasons disclosed must relate to the factors reviewed judgmentally, even if the factors were also considered in the credit scoring component.

For example – denied due to 'stability of income.' The consumer's contract type of employment has shown unstable income, or the underwriter cannot determine exactly how much the borrower earns. The consumer's credit score may have been considered for a non-QM loan but that was not the reason for denial.

If the application is not approved or denied as a result of the credit scoring, but falls into a gray area, and the creditor performs a judgmental assessment and denies the credit after that assessment, the reasons disclosed must come from both components of the system. The same result applies where a judgmental assessment is the first component of the combined system. The primary reason for denial should be listed first in the statements of denial.

Automatic denial

Some credit decision methods contain features that call for automatic denial because of one or more negative factors in the applicant's record. **For example** - the applicant's previous poor credit history with that creditor, the applicant's declaration of bankruptcy was too recent to application date, or the fact that the applicant is a minor. When a creditor denies the credit request because of an automatic-denial factor, the creditor must disclose that specific factor.

 ©All Rights Reserved

Combined ECOA-FCRA disclosures

Both federal regulations govern the creditors method of providing a consumer with a notice of credit denial. ECOA requires disclosure of the principal reasons for denying or taking other adverse action on an application for an extension of credit. The Fair Credit Reporting Act (FCRA) requires a creditor to disclose when it has based its decision in whole or in part on information from a source other than the applicant or its own files. This Adverse Action Notice combines the requirements so one Notice may be provided to satisfy both regulations.

Disclosing the key factors that adversely affected the consumer's credit score should not be confused with the ECOA requirement to disclose specific reasons for denying or taking adverse action on an application or extension of credit.[4]

Additional Statement of Specific Reasons Requirements

When a consumer's adverse action in whole or in part is related to their credit score, the regulations require that the lender disclose the credit score used. The MMC examiners found some mortgage lenders failed to disclose the credit score it used in taking adverse action along with related information, including up to four key factors that adversely affected the consumer's credit score.[5]

Statements that the adverse action was based on the creditor's internal standards or policies or that the applicant, joint applicant, or similar party failed to achieve a qualifying score on the creditor's credit scoring system are insufficient.[6]

A notification given to an applicant when adverse action is taken must be in writing and contain a statement of the action taken. The required information includes the name and address of the creditor, a statement of the provisions, the name and address of the Federal agency that administers compliance with respect to the creditor, and either:[7]

- A statement of specific reasons for the action taken; or
- A disclosure of the applicant's right to a statement of specific reasons within 30 days if the statement is requested within 60 days of the creditor's notification.

[4] https://www.consumerfinance.gov/rules-policy/regulations/1002/9/#9-b-2-Interp-9
[5] ECOA - 12 C.F.R. §1002.9(b)(2)
[6] interpretation of Paragraph 9(b)(2). in Supplement I
[7] https://www.consumerfinance.gov/rules-policy/regulations/1002/9/#a-2

 ©All Rights Reserved

Fair Credit Reporting Act Fee Compliance

The Fair Credit Reporting Act (FCRA) provides regulations for the fees allowed to be collected for a credit report when used to make a credit decision. The MMC examiners found in the MMEs audits that the credit report fees charged to the borrowers appeared to contain prohibited fees for rapid recheck or expedited rescore.[8] The Fair Credit Reporting Act prohibits a mortgage company from charging the borrower a fee for a "rapid recheck or expedited rescore." Citation violations to lenders were for charging credit report fees to the borrowers that included prohibited fees for rapid recheck or expedited rescore.[9]

Credit reports are important for consumers and can affect their ability to obtain credit, employment, and housing. The credit bureaus are a for profit company. The regulations have been established to determine how a consumer may obtain free review of their credit report, without charge.

The regulations do not allow the consumer to be charged when disputing information on their credit report. A consumer has a right to dispute the accuracy of their credit report and request an investigation of disputed information. If the Credit Bureau finds a reinvestigation is required, there are rules they must follow on managing the dispute.

If the completeness or accuracy of any item of information contained in a consumer's file at a consumer reporting agency is disputed by the consumer and the consumer notifies the agency directly of such dispute, the agency must reinvestigate **free of charge** and record the current status of the disputed information or delete the item from the file in accordance with the regulations. This review must be completed before the end of the 30-day period beginning on the date on which the agency received the notice of the dispute from the consumer.

When a Mortgage Loan Originator decides to order a rapid rescore or other method to expedite the process of correcting credit report errors or updates, the mortgage lender must directly absorb these fees as their expense and may not pass the costs to the individual consumer needing the rescore. The lender may indirectly charge consumers these fees as an aggregate amount for the creditor's overall credit report cost, provided the aggregate amount is reasonable and customary for a credit report.

---

[8] FCRA - 15 U.S.C. §1681i(a)(1)(A)
[9] 15 U.S.C. § 1681i(a)(1)(A)

 ©All Rights Reserved

Free Credit Report Under Some Circumstances

Upon the request of the consumer, a consumer reporting agency shall make all required credit disclosures once during any 12-month period without charge to that consumer if the consumer certifies in writing that the consumer -

(1) is unemployed and intends to apply for employment in the 60-day period beginning on the date on which the certification is made
(2) is a recipient of public welfare assistance; or
(3) has reason to believe that the file on the consumer at the agency contains inaccurate information due to fraud.[10]

Equal Credit Opportunity Act (ECOA) Appraisal Requirement

For decades consumers have had the right to a copy of the appraisal report for the property they used as security for their home mortgage loan. The Equal Credit Opportunity Act (ECOA) states the timing for this requirement and requires the borrower to receive an application disclosure notifying them of their appraisal rights.

The MMC examiners found in the MMEs examinations, they failure to provide the ECOA required copy of the appraisal and applicable valuation disclosures within three business days of application. The violation cited failure to deliver a right to copy of appraisal notice in writing, and files did not have compliant proof of appraisal delivery to the borrower.

ECOA Appraisal Disclosure Notice

In the event an appraisal is required on a loan, the lender is required to provide the "Notice of Right to Receive a Copy of Appraisal." This notice advises the consumer they will receive a copy of the appraisal upon completion, and in any event, no less than three business days prior to consummation. The disclosure also gives the borrower the information they have the right to waive receipt of the appraisal three business days prior to closing.[11]

Multiple Versions of Appraisal Compliance

Often a mortgage lender will request more than one property evaluation completed on a file as a second opinion or a quality control review.

[10] https://www.govinfo.gov/content/pkg/USCODE-2022-title15/pdf/USCODE-2022-title15-chap41-subchapIII-sec1681j.pdf
[11] ECOA - 12 C.F.R. §1002.14(a)(1

 ©All Rights Reserved

For example - When an automated valuation is completed for internal checks and reviews, the borrower is entitled to receive these additional evaluations as well as the full appraisal report completed by an appraiser. The loan file must retain proof that all valuations obtained and used in determining a loan decision secured by a dwelling were provided. The loan file must document this for compliance.

Proof of Appraisal Receipt

Loan files must contain proof the appraisal was delivered to the borrower in compliance with the timing required. The MMC examination discovered MME loan files did not indicate the borrowers were provided with a copy of the appraisal report or other valuation. The loan files are required to document when the applicant was provided a copy of all appraisals and other written valuations developed in connection with an application as required by this regulation.[12]

Complying with ECOA requires a creditor to provide an applicant with a copy of **all appraisals** and other written valuations developed in connection with an application for credit that is to be secured by a first lien on a dwelling. The Bureau of Consumer Financial Protection's (CFPB's) enforces Regulation B that requires a creditor to mail the appraisal report to the applicant, not later than the third business day after receipt.[13]

CFPB official interpretation requires the lender to handle multiple versions of appraisals or valuations to comply with the "all" reference does not refer to all versions of the same appraisal or other valuation. If a creditor has received multiple versions of an appraisal or other written valuation, the creditor is required to provide only a copy of the latest version received.

If, however, a creditor already has provided a copy of one version of an appraisal or other written valuation to an applicant, and the creditor later receives a revision of that appraisal or other written valuation, then the creditor also must provide the applicant with a copy of the revision to comply with the regulations. If a creditor receives only one version of an appraisal or other valuation that is developed in connection with the applicant's application, then that version must be provided to the applicant to comply with the regulations.[14]

---

[12] ECOA - 12 C.F.R. §1002.14(a)(1)
[13] Regulation B, 12 C.F.R. 1002.14(a)(1)
[14] https://www.consumerfinance.gov/rules-policy/regulations/1002/14/#14-a-1-Interp-7

 ©All Rights Reserved

CFPB Appraisal Requirement Official Interpretation

The CFPB has official interpretations on their website providing information for how to comply with this section of ECOA. This is a review of their statements for ECOA appraisal compliance.

A creditor must provide an applicant with a copy of all appraisals and other written valuations developed in connection with an application for credit that is to be secured by a first lien on a dwelling. A creditor shall provide a copy of **each such appraisal or other written valuation promptly upon completion, or three business days prior to consummation of the transaction** (for closed-end credit) **or account opening** (for open-end credit), whichever is earlier. Lenders must comply with Electronic Consent and Signing Act (E-Sign Act) regulations to send by an appraisal to the consumer by email.[15]

For ECOA federal regulations, the term "dwelling" means a residential structure that contains one to four units whether or not that structure is attached to real property. The term includes, but is not limited to, an individual condominium or cooperative unit, and a mobile or other manufactured home.[16]

Motor vehicles are not covered in this definition of dwelling. This ECOA appraisal requirement covers applications for credit to be secured by a first lien on a dwelling whether the credit is for a business purpose (**for example**, a loan to start a business) or a consumer purpose (**for example**, a loan to purchase a home).

For ECOA, an "appraisal or other written valuation" includes, without limitation, an appraisal or other valuation received or developed by the creditor in paper form (hard copy); electronically, such as CD or email; or by any other similar media.

Appraisal Timing Requirement

For ECOA, compliant timing requires that the creditor "provide" copies of appraisals and other written valuations to the applicant "promptly upon completion," or no later than three business days before consummation (for closed-end credit) or account opening (for open-end credit), whichever is

[15] Regulation B, 12 C.F.R.§1002.14(a)(5)
[16] https://www.consumerfinance.gov/rules-policy/regulations/1002/14/#b-2

©All Rights Reserved

earlier.[17] For purposes of this timing requirement, "provide" means "deliver." Delivery to or actual receipt by the applicant by electronic means must comply with the E-Sign Act.

Some lenders have struggled with proper notation in the files to prove the appraisals were sent in a timely manner and in compliance with the regulations. In addition, they struggle to understand the regulations as interpreted.

Question - Should the lender send the appraisal when initially received from the appraiser, or after the underwriter has reviewed, requested revisions, and appraisal report corrections are updated?

According to CFPB interpretation, the application and meaning of the "promptly upon completion" standard depends upon the facts and circumstances, including but not limited to when the creditor receives the appraisal or other written valuation, and the extent of any review or revision after the creditor receives it. "Completion" of the appraisal occurs when the last version is received by the creditor, or when the **creditor has reviewed and accepted the appraisal** or other written valuation to include any changes or corrections required, whichever is later.

Answer - The lender should send the appraisal after the underwriter has accepted the last version of the appraisal which is considered completion by CFPB.

In a transaction that is being consummated (for closed-end credit) or in which the account is being opened (for open-end credit), if an appraisal or other written valuation has been developed but is not yet complete, the three business days before consummation or account opening still applies, unless the applicant waives that deadline as provided. If an applicant waives their right to copy the appraisal report before closing, a copy of the appraisal must be provided at or before consummation or account opening.

Waiver Requirements

ECOA regulation B permits the applicant to waive the receipt of the appraisal timing requirement if the creditor provides appraisal copies at or before consummation or account opening, except where otherwise prohibited by law. Understand state laws governing the property that may not allow waiving of this right.

---

[17] Regulation B, 12 C.F.R Section §1002.14(a)(1)

 ©All Rights Reserved

An allowable waiver must be obtained at least three business days prior to consummation or account opening unless the waiver pertains solely to the applicant's receipt of a copy of an appraisal or other written valuation that contains only clerical changes from a previous version of the appraisal or other written valuation provided to the applicant.

CFPB provided their official interpretation on waiving of the appraisal compliance. Except where otherwise prohibited by law, an applicant's waiver is effective under either of the following two situations:

1. If no later than three business days prior to consummation or account opening, the applicant provides the creditor an affirmative oral or written statement waiving the timing requirement: or
2. If, within three business days of consummation or account opening, the applicant provides the creditor an affirmative oral or written statement waiving the timing requirement and the waiver pertains solely to the applicant's receipt of a copy of an appraisal or other written valuation that contains only clerical changes from a previous version of the appraisal already provided to the applicant three or more business days prior to consummation or account opening. For the purpose of this second type of waiver, revisions will only be considered to be clerical in nature if they have no impact on the estimated value and have no impact on the calculation or methodology used to derive the estimate. In addition, the applicant still must receive the copy of the appraisal revision at or prior to consummation or account opening.[18]

In the past, mortgage lenders were fined for using the appraisal waiver as a standard application disclosure. This standard procedure to have all applicants waive their rights is not allowed, as the mortgage lender is taking the consumer's rights away as part of their daily business procedures. A waiver of the time frame required should be used sparingly and only when the borrower has a hardship if they are required to wait three business days before consummation. The benefit must be to the consumer and not the mortgage lender.

[18] ECOA 12 C.F.R. Section §1002.14(a)(1)

 ©All Rights Reserved

No Transaction Closed Requirement

Even if the transaction will not be consummated (for closed-end credit) or the account will not be opened (for open-end credit), the copy must be provided "promptly upon completion" unless waived as provided. In this case, the copy must be provided to the applicant no later than 30 days after the creditor determines the transaction will not be consummated or the account will not be opened. For compliance, loan files must be documented as to when the appraisal was provided to the consumer.

Compliant and Noncompliant Scenario Examples -

1. On day fifteen after receipt of the application, the creditor's underwriting department reviews an appraisal and determines it is acceptable. One week later, the creditor sends a copy of the appraisal to the applicant. The applicant actually receives the copy more than three business days before the date of consummation (or account opening). The creditor has provided the copy of the appraisal promptly upon completion. This is an example of sending a copy of an appraisal within a week of completion with sufficient time before consummation (or account opening for open-end credit).
2. An appraisal is being revised, and the creditor does not receive the revised appraisal until day forty-five after the application, when the creditor immediately determines the revised appraisal is acceptable. A week later, the creditor sends a copy of the revised appraisal to the applicant and does not send a copy of the initial appraisal to the applicant. The applicant actually receives the copy of the revised appraisal three business days before the date of consummation (or account opening). The creditor has provided the appraisal copy promptly upon completion. This is an example of sending a copy of a revised appraisal within a week after completion and with sufficient time before consummation (or account opening for open-end credit).
3. The creditor receives an automated valuation model (AVM) appraisal report on day five after receipt of the application and treats the AVM report as complete when it is received. On day twelve after receipt of the application, the creditor sends the applicant a copy of the valuation. The applicant actually receives the valuation more than three business days before the date of consummation (or account opening). The creditor has provided the copy of the AVM report promptly upon completion. This is an example of sending a copy of an AVM report within a week after its receipt and with sufficient time before consummation (or account opening for open-end credit).

 ©All Rights Reserved

4. On day twelve after receipt of the application, the creditor's underwriting department reviews an appraisal and determines it is acceptable. Although the creditor has determined the appraisal is complete, the creditor waits to provide a copy to the applicant until day forty-two, when the creditor schedules the consummation (or account opening) to occur on day fifty. The creditor has not provided the copy of the appraisal promptly upon completion. This is an example of a violation of an unacceptable delay in sending an appraisal.
5. The creditor receives an AVM report on day five after application and completes its review of the AVM report the day it is received. The creditor also has ordered a full written appraisal report, but the initial version of the full appraisal received by the creditor is found to be deficient and is sent for review. The creditor waits 30 days to provide a copy of the completed AVM report, until the full appraisal is revised on day thirty-five. The creditor then provides the applicant with copies of the AVM report and the revised full appraisal. While the full appraisal report was provided promptly upon completion, the AVM report was not. This is an example of a violation for unacceptable delay in sending an AVM report while waiting for completion of a second valuation.

Truth-in-Lending (TILA) Right of Recission Compliance

The Truth-in-Lending (TILA) Regulation Z governs owner occupied home loans secured by primary dwellings. When a homeowner obtains a mortgage secured by their primary residence, additional rights are provided by Regulation Z. The MMC examiners found in their examinations, MMEs were not properly providing borrowers with their Regulation Z required notice of the right to rescind.

Regulations require a lender to provide two copies of the notice of the right to rescind to each consumer entitled to rescind which must clearly and conspicuously disclose the date the rescission period expires. The consumer may exercise the right to rescind until midnight of the third business day following consummation, delivery of the notice, or delivery of all material disclosures, whichever occurs last.

Consumer's Right to Rescind Notice

All borrowers with an interest in the property have a right to receive two copies of the Notice of Right to Rescind, but it only takes one borrower with rights to the property to sign the notice to rescind the entire loan transaction. One copy to each entitled consumer is acceptable when the notice is delivered in electronic form in accordance with the consumer’s consent and the E-Sign Act. Rescinding the loan transaction, voids the entire transaction.

 ©All Rights Reserved

The loan files must contain proof the lender complied by providing the borrower the notice. If the required notice or material disclosures are not delivered, the right to rescind then expires three years after consummation, upon transfer of all of the consumer's interest in the property, or upon sale of the property, whichever occurs first. In the case of certain administrative proceedings, the rescission period may be extended in accordance with Regulations.[19]

For this regulation the term "material disclosures" means the required disclosures of the annual percentage rate, the finance charge, the amount financed, the total of payments, the payment schedule, and the disclosures and limitations allowed.[20]

CFPB Regulation Z Right of Rescission Interpretation

CFPB is the regulator for TILA and has provided official interpretations for how to comply with TILA Regulation Z's right of recission. The rescission period within which the consumer may exercise the right to rescind runs for three business days from the last of three events:[21]

1. Consummation of the transaction
2. Delivery of all material disclosures
3. Delivery to the consumer of the required rescission notice

For example –

1. If a transaction is consummated on Friday, June 1, and the disclosures and notice of the right to rescind were given on Thursday, May 31, the rescission period will expire at midnight of the third business day after June 1 - that is, Tuesday, June 5.
2. If the disclosures are given and the transaction consummated on Friday, June 1, and the rescission notice is given on Monday, June 4, the rescission period expires at midnight of the third business day after June 4 - that is, Thursday, June 7.

To rescind, the consumer must place the rescission notice in the mail, email it, or deliver it to the creditor's place of business within the waiting period in order to exercise the right. Generally, a lender

[19] TILA- section 125(f) of the Act
[20] 12 C.F.R §1026.32(c) and (d) and §1026.43(g)
[21] https://www.consumerfinance.gov/rules-policy/regulations/1026/23/#23-a-3-Interp-3-ii

 ©All Rights Reserved

will accept any notice to void the transaction, even after the waiting period as the penalty for non-compliance is steep.

Material disclosures must be provided before the rescission timing period can begin to run. Failure to provide information regarding the annual percentage rate (APR) also includes failure to inform the consumer of the existence of a variable rate feature. Failure to give the other required disclosures does not prevent the running of the rescission period, although that failure may result in civil liability or administrative sanctions.[22]

Unexpired Right of Rescission

As provided, the three-year limit may be extended by an administrative proceeding to enforce the provisions of this section. A partial transfer of the consumer's interest, such as a transfer bestowing co-ownership on a spouse, does not terminate the right of rescission.

When the creditor has failed to take the action necessary to start the three-business day rescission period running, the right to rescind automatically lapses on the occurrence of the earliest of the following three events:

1. The expiration of three years after consummation of the transaction.
2. Transfer of all the consumer's interest in the property.
3. Sale of the consumer's interest in the property, including a transaction in which the consumer sells the dwelling and takes back a purchase money note and mortgage or retains legal title through a device such as an installment sale contract.

Transfer of all the consumers' interests includes such transfers as bequests and gifts. A sale or transfer of the property need not be voluntary to terminate the right to rescind.[23]

For example - a foreclosure sale would terminate an unexpired right to rescind. As provided, the three-year limit may be extended by an administrative proceeding to enforce the provisions of this section. A partial transfer of the consumer's interest, such as a transfer bestowing co-ownership on a spouse, does not terminate the right of rescission.

---

[22] TILA 12 C.F.R Section §1026.23(a)(3)(ii)
[23] TILA 12 C.F.R Section §1026.23(b)

 ©All Rights Reserved

Failure to Properly Provide Rescission Notice

The MMC examiners found MMEs failed to not only provide two copies of the notice but failed to provide the notice of right to rescission to all applicants with an interest in the property. Providing notice to the primary borrower only is not acceptable. Regulation Z requires that in a transaction subject to rescission, a creditor must deliver two copies of the notice of the right to rescind to each consumer entitled to rescind, based on ownership interest in the property.

The notice must identify the transaction or occurrence and clearly and conspicuously disclose the following:[24]

- The retention or acquisition of a security interest in the consumer's principal dwelling.
- The consumer's right to rescind the transaction.
- How to exercise the right to rescind, with a form for that purpose, designating the address of the creditor's place of business.
- The effects of rescission.
- The date the rescission period expires.

The notice must include all the above information and the transaction identified by providing the date of the transaction.[25] The CFPB provides model forms for lenders to use in whole or in part provided it meets the regulation minimum requirements and a clear manner.

Unless a consumer waives the right of rescission, no money must be disbursed other than in escrow, no services shall be performed, and no materials delivered until the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded.[26]

TILA Disclosure Zero Tolerance Compliance

TILA requires lenders to disclose all loan transaction fees in a Loan Estimate (LE) with lender origination fees having zero tolerance for change. The MMC examination discovered MME loan files disclosed fees charged to the borrower on the final Closing Disclosure (CD) exceeded the allowable

[24] Regulation Z, 12 C.F.R Section §1026.23(b)
[25] TILA 12 C.F.R Section §1026.23(b)
[26] https://www.consumerfinance.gov/rules-policy/regulations/1026/23/#b-2

 ©All Rights Reserved

tolerances. The loan files did not support any change of circumstance that would have validated the additional charge.[27]

An estimated closing cost disclosed on the Closing Disclosure is not in good faith if the charge paid by or imposed on the consumer exceeds the amount originally disclosed in accordance with the regulations.[28] In a closed-end consumer credit transaction secured by real property or a cooperative unit, other than a reverse mortgage, the creditor must provide the consumer with good faith estimate of the fees for the transaction.[29] For this purpose, the Loan Estimate is used at time of application and the Closing Disclosure is provided at closing.

CFPB Mortgage Broker Compliance

If a mortgage broker receives a consumer's application, either the creditor or the mortgage broker must provide a consumer with the TILA disclosures. If the mortgage broker provides the required disclosures, then mortgage broker must comply with all relevant requirements of TILA. The creditor funding the loan must ensure that such Broker supplied the required disclosures in accordance with the regulations. Disclosures provided by a mortgage broker satisfy the creditor's obligation, but the funding lender is held accountable for TILA compliance.[30]

An estimated closing cost disclosure is in good faith if the charge paid by or imposed on the consumer does not exceed the amount originally disclosed, except as otherwise provided in the regulations.

TILA Good Faith Determination

TILA provides the general rule that an estimated closing cost disclosed is not in good faith if the charge paid by or imposed on the consumer for origination expenses exceeds the amount originally disclosed. Although the regulations allow for some exceptions to the general rule, the charges that may not change after initial disclosure on the Loan Estimate generally include, but are not limited to, the following:

1. Fees paid to the creditor.

---

[27] TILA 12 C.F.R. Section §1026.19(e)
[28] TILA 12 C.F.R. Section §1026.19(e)
[29] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#g-2-iv
[30] TILA 12 C.F.R. Section §1026.37

 ©All Rights Reserved

2. Fees paid to a mortgage broker.
3. Fees paid to an affiliate of the creditor or a mortgage broker.
4. Fees paid to an unaffiliated third party if the creditor did not permit the consumer to shop for a third-party service provider for a settlement service.
5. Transfer taxes.[31]

Charges "paid by or imposed on the consumer" refers to the final amount for the charge paid by or imposed on the consumer at consummation or settlement, whichever is later.

"Consummation" is defined by governing state law, but when a contractual obligation on the consumer's part is created is a matter to be determined under applicable law; Regulation Z does not make this determination.

For example - A contractual commitment agreement that under applicable law binds the consumer to the credit terms would be consummation. Consummation, however, does not occur merely because the consumer has made some financial investment in the transaction (**for example**, by paying a nonrefundable fee) unless, of course, applicable law holds otherwise.[32]

Credit v. sale further defines that consummation does not occur when the consumer becomes contractually committed to a sale transaction unless the consumer also becomes legally obligated to accept a particular credit arrangement.

For example - When a consumer pays a nonrefundable deposit to purchase an automobile, a purchase contract may be created, but consummation for purposes of the regulation does not occur unless the consumer also contracts for financing at that time.

"Settlement" is defined in Regulation Z to means the process of executing legally binding documents regarding a lien on property that is subject to a federally related mortgage loan. This process may also be called "closing" or "escrow" in different jurisdictions.[33]

For example - At consummation, the consumer pays the creditor $100 for recording fees. Settlement of the transaction concludes five days after consummation, and the actual recording fees

---

[31] TILA 12 CFR Section §1026.19(e)(3)(i)
[32] https://www.consumerfinance.gov/rules-policy/regulations/1026/2/#a-12
[33] Regulation X, 12 CFR Section §1024.2(b)

©All Rights Reserved

are $70. The creditor refunds the consumer $30 immediately after recording. The recording fee paid by the consumer is $70.

When fees are "paid to" a person, a fee is not considered "paid to" a person if the person does not retain the fee.

For example - if a consumer pays the creditor transfer taxes and recording fees at the real estate closing and the creditor subsequently uses those funds to pay the county that imposed these charges, then the transfer taxes and recording fees are not considered "paid to" the creditor. There is a difference between transfer taxes and recording fees for this discussion.

Similarly, if a consumer pays the creditor an appraisal fee in advance of the real estate closing and the creditor subsequently uses those funds to pay another party for an appraisal, then the appraisal fee is not "paid to" the creditor for the TILA regulation purposes. A fee is also not considered "paid to" a person if the person retains the fee as reimbursement for an amount it has already paid to another party. If a creditor pays for an appraisal in advance of the real estate closing and the consumer pays the creditor an appraisal fee at the real estate closing, then the fee is not "paid to" the creditor, even though the creditor retains the fee, because the payment is a reimbursement for an amount already paid by the lender.[34]

CFPB Lender Credit Compliance

The disclosure of "lender credits" represents the sum of non-specific lender credits and specific lender credits. Non-specific lender credits are generalized payments from the creditor to the consumer that do not pay for a particular fee on the disclosures provided. Specific lender credits are specific payments, such as a credit, rebate, or reimbursement, from a creditor to the consumer to pay for a specific fee. Non-specific lender credits and specific lender credits are negative charges to the consumer. The actual total amount of lender credits, whether specific or non-specific, provided by the creditor that is less than the estimated "lender credits" identified in the disclosure is an increased charge to the consumer for purposes of determining good faith.

For example - If the creditor discloses a $750 estimate for "lender credits", but only $500 of lender credits is actually provided to the consumer, the creditor has not complied with the regulations

[34] TILA 12 CFR Section §1026.19(e

 ©All Rights Reserved

because the actual amount of lender credits provided is less than the estimated "lender credits" disclosed. This change increases the charge to the consumer for purposes of determining good faith.

However, if the creditor discloses a $750 estimate for "lender credits" to cover the cost of a $750 appraisal fee, and the appraisal fee subsequently increases the appraisal fee by $150, and the creditor increases the amount of the lender credit by $150 to pay for the increase, the credit is not being revised in a way that violates the requirements. Although the credit increased from the amount disclosed, the amount paid by the consumer did not.

However, if the creditor discloses a $750 estimate for "lender credits" to cover the cost of a $750 appraisal fee, but subsequently reduces the credit by $50 because the appraisal fee decreased by $50 to $700, then the requirements have been violated because, although the amount of the appraisal fee decreased, the amount of the lender credit decreased. The reduced appraisal fee cost should be a benefit to the borrower, not the lender.[35]

For purposes of conducting the good faith analysis required by the regulation for lender credits, the total amount of lender credits, whether specific or non-specific, provided to the consumer is compared to the amount of the "lender credits" identified in the regulations. The total amount of lender credits provided to the consumer is determined by aggregating the amount of the "lender credits" identified with the amounts paid by the creditor that are attributable to a specific loan cost or other cost disclosed.

CFPB TILA 10% Tolerance Charges

As allowed in TILA, the lender is allowed to increase some allowable charges within limits. An estimate of a charge for a third-party service or a recording fee is in good faith if:

1. The aggregate amount of charges for third-party services and recording fees paid by the consumer does not exceed the aggregate amount of such charges disclosed that allow limited increases of not more than ten percent.
2. The charge for the third-party service is not paid to the creditor or an affiliate of the creditor; and

[35] TILA 12 CFR Section §1026.37(g)(6)(ii)

 ©All Rights Reserved

3. The creditor permits the consumer to shop for the third-party service as permitted in the regulation.[36]

TILA Regulations provides that certain estimated charges are in good faith if the sum of all such charges paid by or imposed on the consumer does not exceed the sum of all such charges disclosed by more than ten percent. This section of fees on the Loan Estimate permits limited increases for only the following items:

- Fees paid to an unaffiliated third party if the creditor permitted the consumer to shop for the third-party service, consistent with the regulations.
- Recording fees.

Whether an individual estimated charge is in good faith depends on whether the sum of all charges in this section increases by more than ten percent, regardless of whether a particular charge increases by more than ten percent. This is true even if an individual charge was omitted from the estimate provided and then imposed at consummation.

The following examples illustrate the determination of good faith for charges for this section:[37]

- Assume that, in the disclosures provided, the creditor includes a $300 estimated fee for a settlement agent, the settlement agent fee is included in the category of charges, and the sum of all charges in this section (including the settlement agent fee) equals $1,000. In this case, the creditor does not violate TILA if the actual settlement agent fee exceeds the estimated settlement agent fee by more than ten percent (i.e., the fee exceeds $330), provided that the sum of all such actual charges does not exceed the sum of all such estimated charges by more than ten percent (i.e., the sum of all such charges does not exceed $1,100).
- Assume that, in the disclosures provided in this section, the sum of all estimated charges subject to the ten percent rule equals $1,000. If the creditor does not include an estimated charge for a notary fee but a $10 notary fee is charged to the consumer, and the notary fee is subject to the ten percent rule, then the creditor does not violate TILA if the sum of all

[36] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#e-3-i
[37] TILA 12 CFR Section §1026.19(e)(3)(ii)(A)

 ©All Rights Reserved

amounts charged to the consumer does not exceed $1,100, even though an individual notary fee was not included in the estimated disclosures provided.[38]

To calculate the aggregate amount of estimated charges to be in good faith, the aggregate amount of estimated charges must reflect charges for services that are actually performed.

For example - Assume that the creditor included a $100 estimated fee for a pest inspection in the disclosures provided and the fee is included in the category of charges allowing a variance, but a pest inspection was not obtained in connection with the transaction. Then for purposes of the good faith analysis required by TILA Regulation Z, the sum of all aggregate allowable charges paid by or imposed on the consumer is compared to the sum of all such charges disclosed, minus the $100 estimated pest inspection fee.[39] The pest inspection fee was not actually performed, so may not be included in determining compliance to the ten percent variation.

TILA No Tolerance Restrictions

Restrictions on Loan Estimate fees do not apply when a consumer is allowed to shop for the service. Services for which the consumer may but does not select a settlement service provider have different requirements for limitations. Good faith is not determined by the ten percent rule when the creditor permits the consumer to shop for a settlement service provider. When the consumer chooses on their own the settlement service provider that is required by the creditor for the mortgage loan transaction, there are no restrictions on the fee changing. If the consumer selects a settlement service provider identified by the creditor on their list, then good faith is determined in the 10% aggregate as allowed in TILA.[40]

For example - If, in the disclosures provided, a creditor discloses an estimated fee for an unaffiliated settlement agent and permits the consumer to shop for that service, but the consumer either does not choose a provider, or chooses a provider identified by the creditor on the written list provided, then the estimated settlement agent fee is included with the fees that may, in aggregate, increase by no more than ten percent for the purposes allowable change of circumstances.

[38] TILA 12 CFR Section §1026.19(e)(3)
[39] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#e-3-ii-C
[40] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#e-3-ii

 ©All Rights Reserved

If, however, the consumer chooses a provider that is not on the written list, then good faith is determined in accordance with TILA may increase. Regardless of whether the amount paid by the consumer exceeds the amount disclosed, the creditor 'in good faith' provided the best information reasonably available when they provided the disclosure.

The determination of compliance here is whether the creditor allows the consumer to shop. If the creditor is providing a list of providers, that creditor should understand what the settlement service provider will charge within a ten percent variance. Yet if the consumer shops for a settlement service provider, the creditor is not held to have known in advance when quoting the loan fees what this unknown to the creditor third party would charge.

Bona Fide Charges

In covered transactions, TILA requires the creditor to provide the consumer with good faith estimates in the Loan Estimate disclosures. TILA provides that an estimate of the charges is in good faith if it is consistent with the best information reasonably available to the creditor at the time the disclosure is provided and that good faith is determined even if such charges are paid to the creditor or affiliates of the creditor, so long as the charges are bona fide. For determining good faith, to be bona fide, charges must be lawful and for services that are actually performed.[41]

When the settlement service provider does not provide the creditor with their fees, the creditor is obligated to provide the disclosure in the timing required by TILA. The creditor can then use a best guess estimate of what the settlement service provider will charge. When the settlement fees are provided, after disclosure, the creditor may document their file of the issue and provide a change of circumstances revised Loan Estimate.

CFPB Recording Fees Compliance

TILA Regulation Z provides that an estimate of a charge for a third-party service or recording fees is in good faith if the conditions specified are satisfied. Recording fees are not charges for third-party services because recording fees are paid to the applicable government entity where the documents related to the mortgage transaction are recorded. The condition that the creditor permits the consumer to shop for the third-party service is inapplicable. Therefore, estimates of recording fees

[41] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-e-3-iii-Interp-4

©All Rights Reserved

need only satisfy the condition specified in TILA that requires the name of the entity the fees were paid to, and the recording fees for the deed for title ownership transfer are separated from the recording fees for the mortgage or deed of trust.[42]

CFPB Allowable Changes in Fees

TILA Regulation Z does allow some variations for certain charges on the Loan Estimate. An estimate of any of the charges specified is in good faith if it is consistent with the best information reasonably available to the creditor at the time it is disclosed, regardless of whether the amount paid by the consumer exceeds the amount disclosed. Loan fees that the creditor has no control over are not limited by TILA restrictions. For purposes of this part of TILA rules, good faith is determined under this section even if such charges are paid to the creditor or affiliates of the creditor, so long as the charges are bona fide:

1. Prepaid interest
2. Property insurance premiums
3. Amounts placed into an escrow, impound, reserve, or similar account
4. Charges paid to third-party service providers selected by the consumer that are not on the list provided in compliance by the creditor
5. Property taxes and other charges paid for third-party services not required by the creditor[43]

According to CFPB, the good faith requirement for prepaid interest, property insurance premiums, and escrowed amounts have unlimited tolerances although the estimates of these fees and premiums placed into an escrow, impound, reserve or similar account must be consistent with the best information reasonably available to the creditor at the time the disclosures are provided. Differences between the amounts of such charges disclosed and the amounts of such charges paid by or imposed on the consumer do not constitute a lack of good faith, so long as the original estimated charge, or lack of an estimated charge for a particular service, was based on the best information reasonably available to the creditor at the time the disclosure was provided.

This means that the fee/cost estimate disclosed in compliance with TILA Regulation Z was obtained by the creditor through due diligence, acting in good faith.

---

[42] TILA 12 CFR Section §1026.19(e)(3)(ii)
[43] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#e-3-iii-D

 ©All Rights Reserved

For example - If the creditor requires homeowner's insurance but fails to include a homeowner's insurance premium on the estimates provided, then the creditor's failure to disclose does not comply with TILA Regulation Z.

However, if the creditor does not require flood insurance and the subject property is located in an area where floods frequently occur, but not specifically located in a zone where flood insurance is required, failure to include flood insurance on the original estimates provided does not constitute a lack of good faith.

Or, if the creditor knows that the loan must close on the 15th of the month but estimates prepaid interest to be paid from the 30th of that month, then the under-disclosure does not comply with TILA Regulation Z.

If however, the creditor estimates consistent with the best information reasonably available that the loan will close on the 30th of the month and bases the estimate of prepaid interest accordingly, but the loan actually closed on the 1st of the next month instead, the creditor complies with TILA Regulation Z.[44] Most creditors will disclose thirty days of interest on initial TILA disclosures, regardless of when the estimated close of escrow is, so they error on the side of caution with an overestimate.

Differences between the amounts of such Loan Estimate charges disclosed and the amounts of such charges paid by or imposed on the consumer do not constitute a lack of good faith, so long as the original estimated charge, or lack of an estimated charge for a particular service, was based on the best information reasonably available to the creditor at the time the disclosure was provided.

For example- If the consumer informs the creditor that the consumer will choose a settlement agent not identified by the creditor on the written list provided, and the creditor discloses an unreasonably low estimated settlement agent fee of $20 when the average prices for settlement agent fees in that area are $150, then the under-disclosure does not comply with TILA Regulation Z and good faith.

For example - If the consumer informs the creditor that the consumer will obtain a type of inspection not required by the creditor, the creditor must include the charge for that item in the Loan

---

[44] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-e-3-iii-Interp-4

©All Rights Reserved

Estimate disclosures. The actual amount of the inspection fee need not be compared to the original estimate for the inspection fee to perform the good faith analysis. The original estimated charge, or lack of an estimated charge for a particular service, complies with TILA Regulation Z if it is made based on the best information reasonably available to the creditor at the time that the estimate was provided.

But, for example - If the subject property is located in a jurisdiction where consumers are customarily represented at closing by their own attorney, even though it is not a requirement, and the creditor fails to include a fee for the consumer's attorney, or includes an unreasonably low estimate for such fee, on the original estimates provided, then the creditor's failure to disclose, or unreasonably low estimation, does not comply with TILA Regulation Z good faith requirement.

Similarly, the amount disclosed for property taxes must be based on the best information reasonably available to the creditor at the time the disclosure was provided.

For example - If the creditor fails to include a charge for property taxes, or includes an unreasonably low estimate for that charge, on the original estimates provided, then the creditor's failure to disclose, or unreasonably low estimation, does not comply with TILA Regulation Z and the charge for property tax would be subject to the good faith determination. [45]

Revised Estimate Change of Circumstances

Changed circumstances cause the estimated charges on the Loan estimate provided to increase or, in the case of estimated charges that allow a variance, cause the aggregate amount of such charges to increase by more than ten percent.

The creditor may issue a revised loan estimate in good faith, and may use the revised estimate of a charge instead of the estimate originally disclosed if the revision is due to any of the following allowable change circumstance reasons:

1. An extraordinary event beyond the control of any interested party or other unexpected event specific to the consumer or transaction.

---

[45] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-e-3-iii-Interp-4

 ©All Rights Reserved

2. Information specific to the consumer or transaction that the creditor relied upon when providing the disclosures required was inaccurate or changed after the disclosures were provided, or
3. New information specific to the consumer or transaction that the creditor did not rely on when providing the original disclosures required.

A changed circumstance may be an extraordinary event beyond the control of any interested party.

For example - A war or a natural disaster would be an extraordinary event beyond the control of an interested party.

A changed circumstance may also be an unexpected event specific to the consumer or the transaction.

For example - If the creditor provided an estimate of title insurance on the disclosures required, but the title insurer goes out of business during underwriting, then this unexpected event specific to the transaction is a changed circumstance.

A changed circumstance may also be information specific to the consumer or transaction that the creditor relied upon when providing the disclosures required and that was inaccurate or changed after the disclosures were provided.

For example - If the creditor relied on the consumer's income when providing the disclosures required, and the consumer represented to the creditor that the consumer had an annual income of $90,000, but underwriting determines that the consumer's annual income is only $80,000, then this inaccuracy in information relied upon is a changed circumstance.

A changed circumstance may also be the discovery of new information specific to the consumer or transaction that the creditor did not rely on when providing the original disclosures required.

For example - If the creditor relied upon the value of the property in providing the disclosures required, but during underwriting a neighbor of the seller, upon learning of the impending sale of the property, files a claim contesting the boundary of the property to be sold, then this new information specific to the transaction is a changed circumstance.

CFPB Examples of Allowable Change of Circumstances

<u>Charges subject to the zero percent tolerance category.</u>

©All Rights Reserved

Assume a creditor provides a $200 estimated appraisal fee, which will be paid to an affiliated appraiser and therefore may not increase for purposes of determining good faith, except as provided in the regulations. The estimate was based on information provided by the consumer at application, which included information indicating that the subject property was a single-family dwelling. Upon arrival at the subject property, the appraiser discovers that the property is actually a single-family dwelling located on a farm. A different schedule of appraisal fees applies to residences located on farms. A changed circumstance has occurred (i.e., information provided by the consumer is found to be inaccurate after the disclosures required were provided), which caused an increase in the cost of the appraisal. Therefore, if the creditor issues a change of circumstances revised disclosure with the corrected appraisal fee, the actual appraisal fee of $400 paid at the real estate closing by the consumer will be compared to the revised appraisal fee of $400 to determine if the actual fee has increased above the estimated fee.

However, if the creditor failed to provide revised disclosures within the three-business day period after discovery of the change of circumstance, then the actual appraisal fee of $400 must be compared to the originally disclosed estimated appraisal fee of $200.[46] In this instance, the creditor would only be able to charge the consumer $200 appraisal fee at closing, and not the actual fee of $400.

<u>Charges are subject to the ten percent tolerance category.</u>

Assume a creditor provides a $400 estimate of title fees, which are included in the category of fees which may not increase by more than ten percent for the purposes of determining good faith, except as provided in the Regulations. During processing, an unreleased lien is discovered, and the title company must perform additional work to release the lien. However, the additional costs amount to only a five percent increase over the sum of all fees included in the category of fees which may not increase by more than ten percent. A changed circumstance has occurred (i.e., new information), but the sum of all costs subject to the ten percent tolerance category has not increased by more than ten percent tolerance.

TILA Regulation Z does not prohibit the creditor from issuing revised disclosures, but if the creditor issues revised disclosures in this scenario, when the closing disclosures required before closing are

---

[46] [46] TILA 12 CFR Section §1026.19(e)(1)(i)

©All Rights Reserved

delivered, the actual title fees of $500 may not be compared to the revised title fees of $500; they must be compared to the originally estimated title fees of $400 because the changed circumstance did not cause the sum of all costs subject in this category to increase by more than ten percent.[47]

Six pieces of information presumed collected, but not required.

TILA Regulation Z requires creditors to deliver the disclosures no later than the third business day after the creditor receives the consumer's application, which consists of the six key pieces of information. A creditor is not required to collect any of the six pieces of information such as the consumer's name, monthly income, social security number to obtain a credit report, the property address, an estimate of the value of the property, or the mortgage loan amount sought.[48]

However, for purposes of determining whether an estimate is provided in good faith, a creditor is presumed to have collected these six pieces of information.

For example - If a creditor provides the disclosures required TILA Regulation Z prior to receiving the property address from the consumer, the creditor cannot subsequently claim that the receipt of the property address is a changed circumstance.[49]

TILA Loan Estimate Not Delivered in Timely Manner by Broker

The MMC examiners found the MMEs were not ensuring the consumer received the initial application disclosures required by TILA Regulation Z in a timely manner after application. As we discussed earlier, when a creditor accepts the mortgage broker handling of the initial disclosure, they accept the disclosures were provided within compliance to the timing requirements of TILA.[50] If any required disclosures are not provided to the consumer in person, the consumer is considered to have received the disclosures three business days after they are delivered or placed in the mail.

The creditors were given a violation for their brokered loan, where the initial Loan Estimate was not provided in a timely manner. In addition, the initial Loan Estimate must be provided no later than the third business day after the receipt of the consumer’s application even though a company is the

---

[47] [47] TILA 12 CFR Section §1026.19(e)(3)(iv)
[48] TILA Regulation Z Section §1026.19(e)(1)(iii)
[49] CFPB Official interpretation of 19(e)(3)(iv)(A)
[50] TILA 12 C.F.R. Section §1026.19(e)(1)

 ©All Rights Reserved

broker and might have established disclosure agreements with the wholesale lender. The responsibility falls on the originators (funding lender).[51]

The creditor is responsible for delivering or placing in the mail the Loan Estimate no later than the third business day after the creditor receives the consumer's application. Federal Regulation states in part that an application consists of the submission of the consumer's name, the consumer's income, the consumer's social security number to obtain a credit report, the property address, an estimate of the value of the property, and the mortgage loan amount sought.[52] Once this information is received by the broker or the creditor, the initial disclosure timing requirement starts.

Except as allowed by the regulations, the creditor must deliver or place in the mail the loan estimate disclosures required no later than the seventh business day before consummation of the transaction.

Waiver of Seven Day Timing Requirement

If the consumer determines that the extension of credit is needed to meet a bona fide personal financial emergency, the consumer may modify or waive the TILA seven-business-day waiting period for early disclosures, after receiving the disclosures required. To modify or waive the waiting period, the consumer must give the creditor a dated written statement that describes the emergency, specifically modifies, or waives the waiting period, and bears the signature of all the consumers who are primarily liable on the legal obligation. Printed forms for this purpose are prohibited.[53]

Whether a bona fide emergency exists is determined by the circumstances of the individual situation. The imminent sale of the consumer's home at foreclosure, where the foreclosure sale will proceed unless loan proceeds are made available to the consumer during the waiting period, is one example of a bona fide personal financial emergency. Each consumer who is primarily liable on the legal obligation must sign the written statement for the waiver to be effective.[54]

Delayed Construction Loan Settlement

In transactions involving new construction, where the creditor reasonably expects that settlement will occur more than sixty days after the initial disclosures required are provided, the creditor may

---

[51] Topic 7: TILA 12 CFR Section §1026.19(e)(1)
[52] Federal Regulation Section §1026.2(a (3)(ii)
[53] Official interpretation of 19(e)(1)(v)
[54] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-e-1-v-Interp-1

 ©All Rights Reserved

provide revised disclosures to the consumer if the original disclosures state clearly and conspicuously that at any time prior to sixty days before consummation, the creditor may issue revised disclosures. If no such statement is provided, the creditor may not issue revised disclosures, except as allowable change of circumstances.

However, if a use and occupancy permit has been issued for the home prior to the issuance of the disclosures required, then the home is not considered to be under construction and the transaction would not be a construction loan to build a home for the purposes of this rule.[55]

If a creditor uses a revised estimate for the purpose of determining good faith, the creditor shall provide a revised version of the disclosures required including any corrected disclosures reflecting the revised estimate within three business days of receiving information sufficient to establish that one of the reasons for revision has occurred.

For example - The following examples illustrate these requirements:

- Assume a creditor requires a pest inspection. The unaffiliated pest inspection company informs the creditor on Monday that the subject property contains evidence of termite damage, requiring a further inspection, the cost of which will cause an increase in estimated settlement charges by more than ten percent. The creditor must provide revised disclosures by Thursday to comply with TILA Regulation Z.[56]
- Assume a creditor receives information on Monday that, because of a changed circumstance, the title fees will increase by an amount totaling six percent of the originally estimated settlement charges subject to the ten percent tolerance. The creditor had received information three weeks before that, because of a changed circumstance, the pest inspection fees increased by an amount totaling five percent of the originally estimated settlement charges. Thus, on Monday, the creditor has received sufficient information to establish a valid reason for revision and must provide revised disclosures reflecting the eleven percent increase by Thursday to comply with TILA Regulation Z tolerances.[57]
- Assume a creditor requires an appraisal. The creditor receives the appraisal report, which indicates that the value of the home is significantly lower than expected. However, the creditor

[55] CFPB interpretation of 19(e)(3)(iv)(F)
[56] TILA 12 CFR Section §1026.19(e)(4)(i)
[57] TILA 12 CFR Section §1026.19(e)(4)(i)

 ©All Rights Reserved

has reason to doubt the validity of the appraisal report. A reason for revision has not been established because the creditor reasonably believes that the appraisal report is incorrect. The creditor then chooses to send a different appraiser for a second opinion, but the second appraiser returns a similar report. At this point, the creditor has received information sufficient to establish that a reason for revision has, in fact, occurred, and must provide corrected disclosures within three business days of receiving the second appraisal report.

- In this example, in order to comply with the regulations, the creditor must maintain records documenting the creditor's doubts regarding the validity of the appraisal to demonstrate that the reason for revision did not occur upon receipt of the first appraisal report.[58]

Relationship Between Loan Estimates and Closing Disclosures

The creditor may not provide a revised version of the loan estimate disclosures required on or after the date on which the creditor provides the required closing disclosures. The consumer must receive any revised version of the initial TILA disclosures no later than four business days prior to consummation. If the revised version of the disclosures required is not provided to the consumer in person, the consumer is considered to have received such version three business days after the creditor delivers or places such version in the mail. If the consumer consents to the E-Sign Act, delivery is considered the same as if it were mailed unless other method is used to identify the consumer has received the email sooner than the 3-business day requirement for mail.

A revised Loan Estimate may not be delivered to the applicant at the same time as the Closing Disclosure. TILA Regulation Z requires that the consumer must receive any revised version of the loan estimate disclosures no later than four business days prior to consummation. However, if a creditor uses a revised estimate for the purpose of determining good faith and permits the creditor to provide the revision in the closing disclosure the creditor may still meet the four-day requirement.

For example -

1. If the creditor is scheduled to meet with the consumer and provide the closing disclosure required on Wednesday, June 3, and the APR becomes inaccurate on Tuesday, June 2, the

[58] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-e-4-i-Interp-1-iii

 ©All Rights Reserved

creditor complies with the requirements by providing the disclosures reflecting the revised APR on Wednesday, June 3. However, the creditor does not comply with the requirements if it provides both a revised version of the loan estimate disclosure reflecting the revised APR on Wednesday, June 3, and also provides the closing disclosures on Wednesday, June 3.

2. If the creditor is scheduled to email the loan estimate disclosures required to the consumer on Wednesday, June 3, and the consumer requests a change to the loan that would result in revised disclosures on Tuesday, June 2, the creditor complies with the requirements by providing the disclosures required reflecting the consumer-requested changes on Wednesday, June 3. However, the creditor does not comply with the requirements if it provides disclosures reflecting the consumer-requested changes using both the revised version of the loan estimate disclosures on Wednesday, June 3, and also the closing disclosures on Wednesday, June 3.
3. Consummation is scheduled for Thursday, June 4. The creditor hand delivers the disclosures required on Monday, June 1, and, on Tuesday, June 2, the consumer requests a change to the loan that would result in revised disclosures but would not require a new waiting period. The creditor is required to provide corrected disclosures reflecting any changed terms to the consumer so that the consumer receives the corrected disclosures at or before consummation. The creditor complies with the requirements by hand delivering or emailing the disclosures reflecting the consumer-requested changes on Thursday, June 4.
4. Consummation was originally scheduled for Wednesday, June 10. The creditor hand delivers or emails the disclosures required on Friday, June 5. On Monday, June 8, the consumer reschedules consummation for Wednesday, June 17. Also on Monday, June 8, the consumer requests a rate lock extension that would result in revised disclosures but would not require a new waiting period. The creditor complies with the requirements by delivering or placing in the mail the disclosures required reflecting the consumer-requested changes on Thursday, June 11. The creditor is required to provide corrected disclosures reflecting any changed terms to the consumer so that the consumer receives the corrected disclosures at or before consummation. The creditor complies with by hand delivering or emailing the disclosures on Thursday, June 11.
    a. Alternatively, the creditor complies by providing the disclosures to the consumer by mail, including by electronic mail, on Thursday, June 11, because the consumer is considered to have received the corrected disclosures on Monday, June 15 (unless the

 ©All Rights Reserved

creditor relies on evidence that the consumer received the corrected disclosures earlier).

5. Consummation was originally scheduled for Wednesday, June 10. The creditor hand delivers the disclosures required on Friday, June 5, and the APR becomes inaccurate on Monday, June 8, such that the creditor is required to delay consummation and provide corrected closing disclosures, including any other changed terms, so that the consumer receives them at least three business days before consummation. Consummation is rescheduled for Friday, June 12. The creditor complies with the requirements by hand delivering or emailing the disclosures reflecting the revised APR and any other changed terms to the consumer on Tuesday, June 9.[59]

CFPB Delivery Timing for Closing Disclosure

Except as provided in the regulations, the creditor must ensure that the consumer receives the closing disclosures required by TILA Regulation Z no later than three business days before consummation. If any required closing disclosure is not provided to the consumer in person, the consumer is considered to have received the disclosures three business days after they are delivered or placed in the mail.[60]

Mail Delivery

TILA Regulation Z provides that, if any disclosures required are not provided to the consumer in person, the consumer is considered to have received the disclosures three business days after they are delivered or placed in the mail. If the creditor delivers the closing disclosures required in person, consummation may occur at any time on the third business day following delivery.

Other Forms of Delivery

Creditors that use electronic mail or a courier other than the United States Postal Service may follow the timing requirements for disclosures provided by mail services.

For example - If a creditor sends a required disclosure via email on Monday, the consumer is considered to have received the disclosure on Thursday, three business days later. The creditor may,

[59] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-e-4-ii-Interp-1-v
[60] CFPB Official interpretation of 19(f)(1)(ii) Timing

 ©All Rights Reserved

alternatively, rely on evidence that the consumer received the emailed disclosures earlier after delivery. The creditor may, alternatively, rely on evidence that the consumer received the disclosures earlier than three business days after mailing, such as by overnight delivery with signature required.[61]

Creditors using electronic delivery methods, such as email, must also comply with TILA timing requirements for when the consumer is thought to have received the disclosures.

For example - If a creditor delivers the required disclosures to a consumer via email, but the creditor did not obtain the consumer's consent to receive disclosures via email prior to delivering the disclosures, then the creditor does not comply with TILA or E-Sign Act.[62]

No fee may be imposed on any person, as a part of settlement costs or otherwise, by a creditor or by a servicer for the preparation or delivery of the closing disclosures required.

Post-Closing Disclosure (CD) Compliance

The MMC examiners found some MMEs were not providing the borrower with post-closing disclosure when there was a change for third party charges. The MMEs were cited for the violation. TILA requires creditors to provide the Post Closing Disclosure with any corrected Title fee so the amount of fees on the Closing Disclosure matches with the final settlement statement.[63]

If during the 30-day period following consummation, an event in connection with the settlement of the transaction occurs that causes the closing disclosures to become inaccurate, and such inaccuracy results in a change to an amount actually paid by the consumer from that amount disclosed, the creditor is required to deliver or place in the mail corrected disclosures not later than 30 days after receiving information sufficient to establish that such event has occurred.[64] The borrower has a right to have in their possession the final closing disclosure of all fees incurred for the transaction.

For example -

1. Assume consummation occurs on a Monday and the security instrument is recorded on Tuesday, the day after consummation. If the creditor learns on Tuesday that the fee charged by the recorder's office differs from that previously disclosed, and the changed fee results in a

[61] TILA 12 CFR Section §1026.19(f)(1)(ii)(A)
[62] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-f-1-iii-Interp-2
[63] TILA 12 CFR Section §1026.19(f)(2)(iii)
[64] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#f-2-ii-B

 ©All Rights Reserved

change in the amount actually paid by the consumer, the creditor complies with TILA Regulation Z by revising the disclosures accordingly and delivering or placing them in the mail no later than 30 days after Tuesday.

2. Assume consummation occurs on a Tuesday, October 1 and the security instrument is not recorded until 15 days after October 1 on Thursday, October 16. The creditor learns on Monday, November 4 that the transfer taxes owed to the State differ from those previously disclosed, resulting in an increase in the amount actually paid by the consumer. The creditor complies by revising the disclosures accordingly and delivering or placing them in the mail no later than 30 days after Monday, November 4.
    a. Assume further that the increase in transfer taxes paid by the consumer also exceeds the amount originally disclosed on the loan estimate making the fee change above the tolerance limitations allowed. The creditor does not violate TILA Regulation Z if the creditor refunds the excess to the consumer no later than 60 days after consummation, and the creditor delivers corrected closing disclosures to reflect the refund of such excess no later than 60 days after consummation. The creditor satisfies these requirements if it revises the disclosures accordingly and delivers or places them in the mail by November 30.
3. Assume consummation occurs on a Monday and the security instrument is recorded on Tuesday, the day after consummation. During the recording process on Tuesday the settlement agent and the creditor discover that the property is subject to an unpaid $500 nuisance abatement assessment, which was not disclosed, and learns that pursuant to an agreement with the seller, the seller will pay the $500 assessment rather than the consumer. Because the $500 assessment does not result in a change to an amount actually paid by the consumer, the creditor is not required to provide a corrected disclosure.
    a. However, the assessment will result in a change to an amount actually paid by the seller from the amount disclosed. The settlement agent must deliver or place in the mail corrected disclosures to the seller no later than 30 days after Tuesday and provide a copy to the creditor as required.
4. Assume consummation occurs on a Monday and the security instrument is recorded on Tuesday, the day after consummation. Assume further that ten days after consummation the municipality in which the property is located raises property tax rates effective after the date on which settlement concludes. TILA Regulation Z does not require the creditor to provide the

 ©All Rights Reserved

consumer with corrected disclosures because the increase in property tax rates is not in connection with the settlement of the transaction.[65]

If during the 30-day period following consummation, an event in connection with the settlement of the transaction occurs that causes the disclosures to become inaccurate, and such inaccuracy results in a change to an amount actually paid by the consumer from that amount disclosed, the creditor must provide the consumer corrected disclosures.

A creditor is not required to provide corrected disclosures if the only changes that would be required to be disclosed in the corrected disclosure are changes to per-diem interest and any disclosures affected by the change in per-diem interest, even if the amount of per-diem interest actually paid by the consumer differs from the amount disclosed. Nonetheless, if a creditor is providing a corrected disclosure for reasons other than changes in per-diem interest and the per-diem interest has changed as well, the creditor must disclose in the corrected disclosures the correct amount of the per-diem interest and provide corrected disclosures for any disclosures that are affected by the change in per-diem interest.[66]

---

[65] TILA Regulation Z, 12 CFR Section §1026.19(f)(2)(iii)
[66] https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#f-2-iii

 ©All Rights Reserved

Module 2 - Ethics

Ethics Lesson Objective:

The student will learn some of the regulations that govern ethical behavior in the mortgage industry. Some of these laws include the Telephone Consumer Protection Act, Whistleblower Regulations, ECOA, Unfair Deceptive Acts and Practices, the Fair Housing Act, and Housing Financial Discrimination Act. The student will have a strong understanding of what actions are prohibited after a review of these federal regulations. The course also reviews with the students current fraud schemes to prepare students to mitigate fraud in the mortgage industry.

Introduction

Ethics is a required topic for annual licensing, and an important part of professional mortgage lending. With the Dodd-Frank Act, Regulators believed licensing mortgage loan originators (MLOs) would achieve success to ensure that responsible, affordable mortgage credit remains available to consumers. Regulators understand reducing uncertainty facilitates compliance and that is why CFPB provides so many examples which we use in our courses.

Most licensed mortgage loan officers (MLOs), manage their business in an ethical manner. A few MLOs do not understand ethics, and the laws that govern their bad behavior. An MLO may believe they are managing their business in an ethical manner but may not be in compliance with some ethics focused federal regulations. All licensees, including individual MLOs, are responsible for performing their daily activities in an ethical and compliant manner.

CFPB Update

To improve the mortgage industry, the Consumer Financial Protection Bureau (CFPB) has increased their capacity for industry education and enforcement actions in 2023. For the first time a team of technologists dedicated to enforcement matters joined the CFPB. This cross-disciplinary team of technology experts has increased the Bureau’s capacity to enforce the law when emerging technologies harm consumers.

The CFPB recently announced they are significantly expanding their enforcement capacity in 2024 to build on their achievements so far. These positions include enforcement attorneys as well as non-attorney positions, including analysts, paralegals, e-litigation support specialists, economists, and

more. These roles are located in the Washington, D.C. headquarters, and for many, in the regional offices in San Francisco, New York, Chicago, and Atlanta.[67]

Telephone Consumer Protection Act

The Telephone Consumer Protection Act (TCPA) was enacted in 1991 to impose restrictions on the use of automatic telephone auto dialing systems (Do Not Call Provision), artificial or pre-recorded voice messages, and fax machines that sent unsolicited advertisements. The Federal Communication Commission (FCC) adopted rules and regulations implementing the TCPA. Different rules and regulations apply on calls placed to homes rather than calls placed to businesses.

For the mortgage industry, CFPB regulates providing consumers the opportunity to opt out of telemarketing and information sharing.[68] The TCPA includes a Telemarketing Sales Rule with a Do Not Call Provision. The Telemarketing Sales Rule prohibits calling a consumer at home who had asked not to be called again.

Telemarketing Sales Rule

The Telemarketing Sales Rule (TSR) gives the consumers a choice about whether they want to receive telemarketing calls and makes it illegal for specified telemarketers to call consumers. This Act expressly prohibits outbound telemarketing calls that deliver a prerecorded message unless the seller has obtained the call recipient's prior signed and written agreement to receive such calls from that seller. To call or solicit a consumer listed on the Do Not Call Registry is a violation.

Some nonprofit organizations, political organizations, telephone surveyors, and charities are exempt from this regulation. The website with detailed information is at https://www.donotcall.gov/, and https://www.ftc.gov/business-guidance .

TCPA Violations and Fines

According to the Federal Trade Commission (FTC), failure to provide any of the required information truthfully and in a "clear and conspicuous" manner, before the consumer pays for the goods or

[67] https://www.consumerfinance.gov/about-us/blog/the-cfpbs-enforcement-work-in-2023-and-what-lies-ahead/
[68] https://www.consumerfinance.gov/rules-policy/regulations/1022/24/

 ©All Rights Reserved

services offered, is a deceptive telemarketing act or practice that violates the TSR and subjects a seller or telemarketer to a civil penalty of $51,744 for each violation.[69]

CFPB Law Enforcement

Under the Consumer Financial Protection Act (CFPA), the CFPB has the authority to take action against institutions that violate consumer financial laws, including the use of unfair acts or practices, misleading or abusive acts, and against those that violate the Telemarketing Sales Regulations.

The CFPB had previously sued these companies to stop their illegal conduct and demand reparations and other compensation. In March 2023, the district court ruled that the defendants violated the advance fee provision of the Telemarketing Sales Rule. This regulation provides a series of protections to consumers related to telemarketing and establishes restrictions on payment for certain goods and services. It also requires credit repair companies to wait up to six months after providing the consumer with documentation that the promised results have been achieved before requesting or receiving payment from the consumer.

CFPB may ban violators from telemarketing or the financial industry for a period of time, or lifetime. They can prohibit other companies from doing business with certain affiliate marketers. These prohibitions will apply even after bankruptcy proceedings are completed.

CFPB required notifications to all remaining customers who were still enrolled using telemarketing. The notice must give the consumer the right to cancel their services, and the process for canceling them.

The CFPB may determine when its victim relief fund can be used to pay those harmed by perpetrators. Many laws allow for civil penalties as well as imposing civil monetary penalties.

Unlawful Junk Fees for Credit Repair Settlements

In August 2023, the CFPB entered into a settlement with a ring of corporate entities operating some of the largest credit repair brands in the country, including Lexington Law and CreditRepair.com. The settlement follows a federal court ruling that the companies violated federal law by collecting billions of dollars in illegal advance fees for credit repair services for many years.[70]

---

[69] https://www.ftc.gov/business-guidance/resources/complying-telemarketing-sales-rule

[70] https://www.consumerfinance.gov/about-us/newsroom/cfpb-acuerda-con-conglomerado-de-reparacion-de-credito/

 ©All Rights Reserved

During the time period relevant to the lawsuit, the companies operated throughout the country and had more than four million customers who were subjected to telemarketing practices. As of 2022, the defendants had combined annual revenues of approximately $388 million. The settlement came after a court ruled that the companies charged illegal upfront fees for credit repair services using telemarketing, violating federal law. If approved, the resolution would impose a judgment of $2.7 billion on these companies. The order would also prohibit these companies from telemarketing credit repair services for ten years.

"*People looking to improve their credit scores across the country have turned to companies like CreditRepair.com and Lexington Law. These credit repair industry giants used bogus real estate and rent-to-own opportunities to illegally lure people in and line their pockets with billions of dollars in fees*," said CFPB Director Rohit Chopra. "*This scam is another sign that we need to work harder to fix the credit scoring and reporting system in our country*."

Following the district court ruling, the companies filed for Chapter 11 bankruptcy protection. The companies stated that they had closed about 80% of their business, including their call centers, and had laid off about nine hundred employees in response to the court ruling.

Whistleblower Regulations

The Consumer Financial Protection Bureau (CFPB) provides some protections for federal employees and applicants that are "whistleblower" with the Whistleblower Protection Act. A "whistleblower" provides information he or she reasonably believes have evidence of:

- A violation of any law, rule, or regulation
- Gross mismanagement
- A gross waste of funds
- An abuse of authority
- A substantial and specific danger to public health or safety

This bill requires the CFPB to provide awards to whistleblowers who report information resulting in monetary sanctions. Whistleblowers claiming an award are permitted to have legal representation.[71]

[71] https://www.ftc.gov/office-inspector-general/whistleblower-protection#:~:text=Overview%20of%20the%20WPA%20%2D%20The,supervisors%20who%20retaliate%20against%20Whistleblowers.

 ©All Rights Reserved

This Act protects federal employees or applicants against retaliation for telling authorities about suspected fraudulent activities. It prohibits federal agencies from taking or threatening a personnel action because an employee or applicant made a whistleblower disclosure.

In addition, mortgage industry personnel may not be retaliated against by their employer when the whistleblower reports wrongdoing to a federal, state, or local government authority or law enforcement agency. If the illegal conduct violates any provisions of Title X of the Dodd Frank Act, and it is reported, they will have whistleblower rights. If they have experienced retaliation, they may report it to the U.S. Occupational Safety and Health Administration.

A whistleblower may request that the Office of Inspector General (OIG) keep their identity confidential. An OIG is prohibited from disclosing an employee's identity without the employee's consent unless the OIG determines that disclosure is unavoidable or is compelled by a court order.[72]

Equal Credit Opportunity Act (ECOA), Regulation B

The Equal Credit Opportunity Act (ECOA) is among the oldest laws to provide guidance for ethical behavior. ECOA prohibits creditors from unethical and illegal discrimination against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (provided the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income was derived from public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. Ethics in the mortgage industry is required for consumers to trust their mortgage professional and lender.

ECOA and Fair Housing Act Prohibitions

Under the ECOA, it is unlawful for a lender to discriminate on a prohibited basis in any aspect of a credit transaction, and under both the ECOA and the Fair Housing Act (FHAct), it is unlawful for a lender to discriminate on a prohibited basis in a residential real estate related transaction. Under one or both of these laws, a lender may not, because of a prohibited factor:

[72] https://www.ftc.gov/office-inspector-general/whistleblower-protection#:~:text=Overview%20of%20the%20WPA%20%2D%20The,supervisors%20who%20retaliate%20against%20Whistleblowers.

 ©All Rights Reserved

- Fail to provide information or services or provide different information or services regarding any aspect of the lending process, including credit availability, application procedures, or lending standards.
- Discourage or selectively encourage applicants with respect to inquiries about applications for credit.
- Refuse to extend credit or use different standards in determining whether to extend credit.
- Vary the terms of credit offered, including the amount, interest rate, duration, or type of loan.[73]
- Use different standards to evaluate collateral.
- Treat a borrower differently in servicing a loan or invoking default remedies.
- Use different standards for pooling or packaging a loan in the secondary market.

A lender may not express, orally or in writing, a preference based on prohibited factors or indicate that it will treat applicants differently on a prohibited basis. A violation may still exist even if a lender treated applicants equally.

A lender may not discriminate on a prohibited basis because of the characteristics of

- An applicant, prospective applicant, or borrower.
- A person associated with an applicant, prospective applicant, or borrower (**for example** - a co-applicant, spouse, business partner, or live-in aide).
- The present or prospective occupants of either the property to be financed or the characteristics of the neighborhood or other area where property to be financed is located.

Finally, the FHAct requires lenders to make reasonable accommodations for a person with disabilities when such accommodations are necessary to afford the person an equal opportunity to apply for credit.[74]

---

[73] https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/4/iv-1-1.pdf
[74] https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/4/iv-1-1.pdf

 ©All Rights Reserved

Discrimination

The Fair Housing Act (FHAct) and the Equal Credit Opportunity Act (ECOA) protect consumers by prohibiting unfair and discriminatory practices. Read the OCC's "Answers About Consumer Loans" and "Answers About Mortgages and Home Loans" for more information.[75]

The FHAct prohibits discrimination in residential real estate–related transactions based on -

- **race or color**
- **national origin**
- **religion**
- **sex**
- familial status
- handicap

ECOA prohibits discrimination in credit transactions based on -

- **race or color**
- **national origin**
- **religion**
- **sex**
- marital status
- age*
- applicant's receipt of income from a public assistance program
- applicant's exercise, in good faith, of any right under the Consumer Credit Protection Act

*Age is a prohibited factor provided the applicant has the capacity to enter into a contract.[76]

Disparate Impact

A lender's policies, even when applied equally to all its credit applicants, may have a negative effect on certain applicants. **For example -** a lender may have a policy of not making single family home loans for less than $60,000. This policy might exclude a high number of applicants who have lower

[75] https://www.occ.treas.gov/topics/consumers-and-communities/consumer-protection/truth-in-lending/index-truth-in-lending.html
[76] https://www.occ.treas.gov/topics/consumers-and-communities/consumer-protection/fair-lending/index-fair-lending.html

©All Rights Reserved

income levels or lower home values than the rest of the applicant pool. That uneven effect of the policy is called disparate impact.

Disparate Treatment

Illegal disparate treatment occurs when a lender bases its lending decision on one or more of the prohibited discriminatory factors covered by the fair lending laws.

For example – An 80-year-old borrower applies for a 30-year fixed mortgage. The creditor's mortgage loan originator pre-approves the loan request but limits the term to 15 years due to his age. The originator reasoned the borrower was a risk to the creditor since he likely would not live long enough to pay back the loan. The decision was not based on the fact the borrower qualified for the 30-year loan. This is 'blatant' age discrimination by the MLO.

The Fair Housing Act

The Fair Housing Act (FHAct) provides guidance for what is considered prohibited for mortgage lenders to consider when requesting financing for a home loan. FHAct prohibits discrimination based on race, color, national origin, religion, sex, familial status, or handicap. Members of a community should not be discouraged or excluded from the lending opportunities available to the masses based purely on a prohibited basis. To do so is considered unethical and predatory mortgage lending. Access to credit is a right for everyone, provided they qualify for the mortgage loan.

For example - A married couple applies for a home loan with the mortgage loan originator. The MLO decides to complete the loan in the wife's name only as she makes the most income. The MLO accepts the loan request and puts it into processing. The next day an unmarried couple comes in for a home loan application with the same loan originator. They both want to be on the loan, but the MLO discourages the couple from making a joint application because they are unmarried. The MLOs personal religion discourages sex outside of marriage, and he feels this would violate his beliefs. The MLO steers the consumers to only apply with one of them explaining it will be better for them to hold title this way since they are not married.

This is discrimination based on familial status, as the MLO treats married couples differently than unmarried couples. It would also be a violation of ECOA based on marital status. By having different requirements, he is limiting the availability of credit to the unmarried couple.

The mortgage loan originator's religious beliefs do not provide him a right to discriminate in residential mortgage lending. The MLO should have the right to have the unmarried couple go to

 ©All Rights Reserved

another MLO in his office if he cannot provide unbiased service to avoid his company from having ECOA and FHAct violations.

Predatory Lending

Fair lending laws also contain provisions to address predatory lending practices.

For example -

- Collateral or equity "stripping": The practice of making loans that rely on the liquidation value of the borrower's home or other collateral rather than the borrower's ability to repay.
- Inadequate disclosure: The practice of failing to fully disclose or explain the true costs and risks of loan transactions.
- Risky loan terms and structures: The practice of making loans with terms or structures that make it more difficult or impossible for borrowers to reduce their indebtedness.
- Padding or packing: The practice of charging customers unearned, concealed, or unwarranted fees.
- Flipping: The practice of encouraging customers to frequently refinance mortgage loans solely for the purpose of earning loan-related fees without a net tangible benefit to the borrower.
- Single-premium credit insurance: The requirement to obtain life, disability, or unemployment insurance for which the consumer does not receive a net tangible financial benefit.

Unfair Deceptive Acts and Practices

Multiple government agencies work to fight fraud and protect consumers. Early on the Office of Comptroller of Currency (OCC) took the lead among the federal bank regulatory agencies in developing an approach to address unfair and deceptive marketing practices. These practices are often an element in predatory lending. The OCC has taken a number of enforcement actions against banks that were found to have engaged in abusive practices and, in one landmark case, required a bank to pay over $300 million in restitution to its customers.

The Housing Financial Discrimination Act

The Housing Financial Discrimination Act requires the Fair Lending Notice disclosure be signed by the borrower. The Fair Lending Notice provides information on acts that are illegal and unethical when determining a consumer’s credit worthiness. The combined disclosure encompasses the consumer rights provided in several Acts (RESPA, ECOA, and FHAct). This legislation identifies what is

 ©All Rights Reserved

considered unethical to use when making a credit decision. FHAct prohibits discrimination in all aspects of "residential real-estate related transactions," including but not limited to:

- Making loans to buy, build, repair, or improve a dwelling
- Purchasing real estate loans
- Selling, brokering, or appraising residential real estate, or
- Selling or renting a dwelling

For example - a mortgage lender decides they are going to stop approving loans in a low income ethic neighborhood because they have experienced too high a delinquency on the loans they produced in this neighborhood. This would be a violation of the Housing Discrimination Act due to using race and trends of a neighborhood to make lending policies unless the lender can justify doing loans in the area are unsound business practice. If the lender not providing loans in the area causes a negative impact to borrowers in this area, this would be considered unethical and unfair lending practices.

Lenders are required to look at all transactions on their own merits for making a credit decision, and not on any of the ECOA or Fair Housing Act prohibited factors.

Unlawfully Discriminatory Lending Practices

<u>Redlining</u>

Red-lining is where a particular neighborhood, zip code, or community are excluded from marketing efforts and/or loan approvals due to reasons that are not based on sound business practice but blatant, disparate-treatment or disparate-impact practices. **Redlining is the practice of denying a creditworthy applicant a loan for housing in a certain neighborhood even though the applicant may otherwise be eligible for the loan.** The term referred to the practice of mortgage lenders drawing red-lines around neighborhoods or census tracts on a map to indicate the unwanted areas to originate mortgage loans.[77]

For example - A mortgage banker that office is in a poor neighborhood may assume the borrowers would be unable to make the loan payments, so target advertising to only affluent areas fifty miles outside their immediate neighborhood. If this policy caused a disparate impact to the neighborhood

---

[77] https://www.federalreserve.gov/boarddocs/supmanual/cch/fair_lend_fhact.pdf

 ©All Rights Reserved

they serve, their policy would be a violation by making it difficult for residents in the neighborhood to obtain home financing.

The prohibition against redlining does not mean that a lending institution is expected to approve all housing loan applications or to make all loans on identical terms. Denying loans or granting loans on more-stringent terms and conditions, however, must be justified on the basis of the borrower creditworthiness and property acceptance; and without regard to the prospective borrower's race, color, religion, national origin, sex, marital status, or **the neighborhood in which the property is located**.

For example - a mortgage lender may consider such economic factors as:

- An applicant's income or credit history - Character
- The condition, use, or design of the proposed security property (or of those nearby properties that clearly affect the value of the proposed security property) – Collateral
- The availability of neighborhood amenities or city services – Collateral
- The need of the lender to hold a balanced real estate loan portfolio, with a reasonable distribution of loans among various neighborhoods, types of property, and loan amounts – Sound business practice.

It would not be sound business practice to be over exposed with a concentration of all business in one neighborhood. Diversified investments in lending may be considered a sound business practice. FHA limits the number of FHA insured condominium loans in a condo project to manage their risk exposure. Each of the factors must be applied without regard to any prohibited factors.

Lowballing

Lowballing is the practice of manipulating property values to obtain an excessively low appraisal in relation to the purchase price on the basis of prohibited considerations which is one form of redlining. Lending more than the appraised value of the collateral is not sound business practice, and lowballing forces a borrower either to cancel the purchase contract, the loan application, or both; or to make a larger down payment on a property in order to make up the difference between the sales price and the low appraised value.

For example - this may allow the lender to have a lower exposure to risk on this home loan since the loan amount was based on the lowballed price and the property is actually valued at a higher

©All Rights Reserved

amount. If the lender did have to foreclosure, they would be more likely to be able to recoup their foreclosure losses. Benefit to the lender, not the consumer.

Racial Steering

Racial steering is deliberately guiding loan applicants or potential purchasers toward or away from certain types of loans or geographic areas because of race. This is a blatant ECOA violation and is illegal.

Application of Different Standards or Procedures

The application of different standards or procedures in administering foreclosures, late charges, penalties, reinstatements, or other collection procedures is unlawful. Collection practices must be fair to all clients and standards applied evenly to all clients.

Discriminatory Acts Have a Negative Impact

The courts have held that discriminatory acts that have a negative impact on non-minorities, such as white individuals, are illegal and that such individuals have standing to sue.

Excessively Burdensome Qualifications

The use of excessively burdensome qualification standards to deny, or that have the effect of denying, housing to minority applicants is also illegal under the FHAct.

Onerous Rates, Terms, Conditions, or Requirements

The imposition of more-onerous interest rates, or other more-onerous terms, conditions, or requirements, on minority loan applicants is explicitly prohibited. The phrase "terms or conditions" as used in the act covers many types of discriminatory practices.

Use of Racially Exclusive Images

The use of racially exclusive images has repeatedly been found to be illegal even when there was little, or no evidence of a discriminatory policy directed toward any given individual. This practice has been held to violate the Fair Housing Act as well.

For example - a housing lender might exploit an exclusive image by showing only applicants of a particular race in advertisements for home loans.

For example - using only white individuals in advertisements for home equity loans may suggest to viewers that 'only white applicants need apply' or 'only people who look like that could afford to have that type of loan.' How would a reasonable consumer view this advertisement?

Advertising must be inclusionary, as you may have noticed most modern-day ads show couples and families that are mixed race, same sex, single parent, and other combinations to include how people see themselves. To attract today's homebuyers and be in compliance with FHAct, mortgage lenders should reach out to the diverse community it serves.

Mortgage lenders are not expected to make unsound mortgage loans or to render services on more-favorable terms to applicants solely because of the applicant's status as a member of a protected class. However, denying loans or services on a prohibited basis is illegal.

Fraud Trend Evolution

According to Experian, the fraud landscape is constantly evolving, and staying vigilant against the latest trends is critical to safeguarding yourself, your organization, and your consumers. In 2023 these were the top fraud trends and their continued potential impact.[78]

When economic uncertainty reigns, a rise in fraud often follows. To begin with, consumers tend to be financially stressed in such periods and prone to making risky decisions. In addition, fraudsters are keenly aware of the opportunities inherent in unstable times and develop tactics to take advantage of them.

For example - As consumers rein in spending and financial institutions struggle to maintain new account volumes, fraudsters might ramp up their new account and loan activities.

Fraud is becoming more sophisticated.

For example - Thanks to the rapid rise in the availability of artificial intelligence (AI) tools, fraudsters are increasingly able to impersonate companies and individuals with ease, as well as consolidate data from diverse sources and use it more efficiently.

---

[78] https://www.experian.com/blogs/insights/biggest-fraud-trends/#:~:text=Fraud%20is%20a%20serious%20concern,of%20concern%20about%20fraud%20risk.

©All Rights Reserved

CFPB Fraud Findings

The CFPB safeguards household financial stability by ensuring that consumer financial markets are fair, transparent, and competitive. Their enforcement authority is among the CFPB's most impactful tools for reinforcing compliance with federal consumer financial laws and sending a clear message to entities within their authority and the public that the CFPB remains vigilant on behalf of consumers.

When a financial institution, individual, or other entity subject to the CFPB's authority breaks the law, the CFPB may take enforcement action against them. As previously discussed, under certain cases, the CFPB may partner with other federal, state, or local agencies to investigate the wrongdoing and coordinate the enforcement action.

In 2023, the CFPB filed twenty-nine enforcement actions and resolved through final orders six previously filed lawsuits. Those orders require lawbreakers to pay approximately $3.07 billion to compensate harmed consumers and pay approximately $498 million in civil money penalties.[79]

Their enforcement actions are public knowledge, but we have left out the individual names for privacy. You may look up more information by following the citation link. Some of their enforcement actions included the following:

- Protecting service members from illegal high-interest loans and false advertising. In this action, a home loan company was banned from the mortgage lending industry.
- Action against a bank for illegally charging junk fees, withholding credit card rewards, and opening fake accounts.
- Action to stop loan churning is a refinancing scheme that repeatedly charged fees eat up the equity.
- Stopped unlawful junk advance fees for credit repair services.

CFPB Possible Future Fraud Risks

It is anticipated that markets in both U.S. and foreign financial services sectors will evolve to address different and ever-changing risk factors based on their programs, unique business mixes, and organizational structures. These future external challenges must be monitored, as they will impact

---

[79] https://www.consumerfinance.gov/about-us/blog/the-cfpbs-enforcement-work-in-2023-and-what-lies-ahead/#:~:text=In%202023%2C%20the%20CFPB%20filed,million%20in%20civil%20money%20penalties.

 ©All Rights Reserved

the work of the CFPB in protecting financial consumers and addressing a continually changing financial environment. It is also anticipated that as CFPB continues to exercise its authorities and regulate the financial services markets, the financial institutions in those markets will continue to contest the CFPB's rules, regulations, and authorities.

In addition, the CFPB's statutory method of funding has been the subject of litigation. On October 3, 2023, the Supreme Court heard oral arguments in CFPB v. Community Financial Services Association of America, in which a three-judge panel of the Fifth Circuit held in October 2022 that the law funding the CFPB's operations through the earnings of the Federal Reserve System violates the Appropriations Clause. To date, all other courts considering this question have upheld the CFPB's statutory funding mechanism, and a decision by the Supreme Court is expected in the first half of calendar year 2024. These contests may also impact the work of the CFPB in the future.[80]

Fraud Motivations

There are two basic motivations for mortgage fraud. Fraud for housing and fraud for profit.

Fraud for Housing

Fraud for Housing primarily consists of illegal actions by borrowers motivated to acquire or maintain ownership of a home. This type of fraud is committed when a borrower materially misrepresents information on a mortgage loan application such as employment, income, or assets in order to obtain a mortgage. The borrower is motivated to acquire ownership of a house.

Some fraud for housing people purchases a home as an owner occupied for a cousin or other close family member, knowing they will not be moving into the property. Creditors have put more conditions on borrowers that are purchasing their second property and retaining their current primary resident because of this fraud issue.[81]

FHA Requirements

If Rental Income is being derived from the Property being vacated by the Borrower, the Borrower must be relocating to an area more than one hundred miles from the Borrower's current Principal

---

[80] https://files.consumerfinance.gov/f/documents/cfpb_final-financial-report-fy_2023-11.pdf, page 51
[81] https://www.fhfa.gov/PolicyProgramsResearch/Programs/Pages/Fraud-Prevention.aspx

 ©All Rights Reserved

Residence. The Mortgagee must obtain a lease agreement of at least one year's duration after the Mortgage is closed and evidence of the payment of the security deposit or first month's rent.[82]

FNMA Requirements

When the borrower owns mortgaged real estate, the status of the property determines how the existing property's PITI must be considered in qualifying for the new mortgage transaction. If the mortgaged property owned by the borrower is -

- an existing investment property or a current principal residence converting to investment use, the borrower must be qualified in accordance with, but not limited to all FNMA policies regarding rental income use, reserve requirements and limits on financed properties.
- an existing second home or a current principal residence converting to a second home, the PITI of the second home must also be counted as part of the borrower's recurring monthly debt obligations.[83]

Fraud for Profit

This type of fraud is a more complex process involving a group of industry insiders attempting to defraud lenders for profit. Those who commit this type of mortgage fraud use their knowledge or authority to commit or facilitate the fraud.

This collusion by industry insiders may include mortgage loan originators, appraisers, mortgage brokers, attorneys, or other professionals engaged in the industry. Fraud for profit aims not to secure housing, but to misuse the mortgage lending process to steal cash and equity from lenders or homeowners.

Fraud for Profit schemes aim to gain cash or home equity through abuse of the mortgage lending process. This is the type of fraud federal agencies target as it does the most damage to consumers and the mortgage industry.[84]

---

[82] https://www.hud.gov/sites/dfiles/OCHCO/documents/4000.1hsgh-011823.pdf
[83] https://selling-guide.fanniemae.com/Selling-Guide/Origination-through-Closing/Subpart-B3-Underwriting-Borrowers/Chapter-B3-6-Liability-Assessment/1032991161/B3-6-06-Qualifying-Impact-of-Other-Real-Estate-Owned-06-30-2015.htm
[84] https://www.fhfa.gov/PolicyProgramsResearch/Programs/Pages/Fraud-Prevention.aspx

©All Rights Reserved

Collusion Issues

Mortgage fraud can occur through the actions of borrowers and through the actions of mortgage industry professionals in connection with obtaining a mortgage loan. Common instances of fraud committed by borrowers and mortgage industry professionals include:

- Providing false information regarding employment status, income level, or employer
- Misrepresenting the source of funds for a borrower's down payment
- Falsifying a borrower's credit score and/or outstanding debts and liabilities
- Misrepresenting a borrower's intent to occupy the property
- Providing false information concerning a borrower's identity
- Using inaccurate appraisal figures to misrepresent the true value of a property
- Obtaining multiple loans on a single property based on false information
- Providing false property information to secure or modify a loan
- Misrepresenting income, hardship, or related information to halt foreclosure or influence a short-sale decision[85]

Impactful Fraud Trends of 2023

The fraud trends that emerged in 2023 were diverse, though they all had one thing in common: fraudsters' ability to take advantage of new technologies and opportunities. Businesses are feeling the repercussions, with nearly 70% reporting that fraud losses have increased in recent years.

Here are five trends Experian forecasted in the fraud and identity space that challenged regulators and mortgage professionals this year. Some of your home loan applicants may fall victim to these types of fraud.

Deposit and Checking Account Fraud

With everyone focused on fraud in the on-line channels, it is interesting that financial institutions reported more fraud occurring at brick-and-mortar locations. Preying on the good nature of helpful branch employees, criminals are taking risks by showing up in person to open accounts, pass bad

[85] https://www.fhfa.gov/PolicyProgramsResearch/Programs/Pages/Fraud-Prevention.aspx

 ©All Rights Reserved

deposits and try to work their way into other financial products. The Treasury Department reports complaints doubling YoY, after increasing more than 150% between 2020 and 2021.

Synthetic Identity Fraud

Not quite fake, not quite real, so-called synthetic or "Frankenstein" identities mash up real data with false information to create unique customer profiles that can outsmart retailers' or financial institutions' fraud control systems. With synthetic identity (SID) fraud, real data is often stolen or purchased on the dark web and combined with other information, even Artificial Intelligence (AI), to created faces so that fraudsters can build up a synthetic identity's credit score before taking advantage of them to borrow and spend money that will never be paid back.

Fake Job Postings and Mule Schemes

Well-paying remote work was in high demand, creating opportunities for fraudsters to create fake jobs to harvest data such as Social Security numbers from unsuspecting applicants. Experian predicts a continued rise in "mule" jobs, in which workers unknowingly sign on to do illegal work, such as re-shipping stolen goods.

According to the Better Business Bureau, an estimated fourteen million people get caught in a fake employment fraud yearly. Job seekers can protect themselves by being skeptical of jobs that ask them to do work that appears suspicious, requires money, financial details, or personal information upfront.

Peer-to-peer Payment Fraud

Peer-to-peer payment tools are increasingly popular with consumers and fraudsters, who appreciate that they are both instant and irreversible. Experian expects to continue to see an increase in fraudulent activity on these payment systems, as fraudsters use social engineering techniques to deceive consumers into paying for nonexistent merchandise or even sharing access credentials. Stay safe while using peer-to-peer payment tools by avoiding common scams like requests to return accidental payments, opting for payment protection whenever possible and choosing other transaction methods like paying with a credit card.

Social Media Shopping Fraud

Social media platforms are eager to make in-app shopping fun and friction-free for consumers, and many brands and shoppers are keen to get on board. In fact, approximately 58% of users in the U.S. have purchased a product after seeing it on social media.

 ©All Rights Reserved

Unfortunately, these tools neglect effective identity resolution and fraud prevention, leaving sellers vulnerable to fraudulent purchases. And while buyers have some recourse when a purchase turns out to be a scam, it is wise to be cautious while shopping on social media platforms by researching sellers, only using credit cards and being cognizant of common scams, like when vendors on Facebook Marketplace ask for payment upfront.

Employer Text Fraud

Fraudulent text messages, also known as "smishing," a mash-up of Short Messaging Service (SMS) and phishing continues to rise. In fact, according to data security company Lookout, 2022 was the biggest year ever for such mobile phishing attacks, with more than thirty percent of personal and enterprise mobile phone users exposed every quarter.

Fraud Prevention and Detection Matter

Nearly two-thirds of consumers say they are "very" or "somewhat concerned" with online security, and more than eighty five percent expect businesses to respond to their identity and fraud concerns. Addressing and preventing fraud and communicating these fraud-prevention actions to customers is an essential strategy for businesses that want to maintain customer trust, thereby decreasing churn and maximizing conversions on new leads.

Fraud Strategy

According to Experian, in 2024 fraud management solutions must be even more technically advanced than the fraudulent techniques they are combating. But more than that, they need to be appealing to consumers, who are likely to abandon signup or purchase attempts when they become too onerous. In fact, 37% of consumers have moved their business elsewhere due to a negative account opening experience.

To succeed, effective fraud strategies must be seamless, low friction, data-driven and customer-focused. That means making use of up-to-date technologies that boost security while prioritizing a positive customer experience.

 ©All Rights Reserved

Experian and other providers have creditor tools for fraud prevention and identity verification tools which help creditors detect and combat fraud. If a company is unable to manage with their own staff, outside companies can provide the service to implement a fraud management solution.[86]

Omnichannel Fraud Report

According to Transunion, globally in 2022 fraud returned to something more closely resembling pre-pandemic levels. However, with increased digital transaction volumes, the risk to organizations and individuals was even greater than before.[87]

Transunion's 2023 State of Omnichannel Fraud Report provided insights and recommendations for implementing smarter, more effective fraud prevention strategies that build consumer trust by demonstrating safety in customer experiences.

Global fraud trends highlighted in the report include:

- Growth in digital transactions is driving fraud risk exposure
- 4.6% of global digital transactions were potentially fraudulent in 2022
- 80% increase in digital transactions resulted in 80% growth in suspected digital fraud attempts globally from 2019 to 2022
- Stolen identifiers are being weaponized to commit increasingly sophisticated fraud
- 83% increase in publicly reported data breaches in the US from 2020 to 2022
- $4.6 billion outstanding balances attributed to suspected synthetic identities for US auto loans, credit cards, retail credit cards and unsecured personal loans (highest level ever and a 27% increase since 2020)
- Fraudsters are using every available digital channel to access consumer accounts
- 62% of high-risk phone calls into US call centers were from non-fixed VoIP phone lines in 2022
- 52% of consumers said they were targeted with online, email, phone call or text messaging fraud attempts from Sept. to Dec. 2022

[86] https://www.experian.com/blogs/insights/biggest-fraud-trends/#:~:text=Fraud%20is%20a%20serious%20concern,of%20concern%20about%20fraud%20risk.
[87] https://www.transunion.com/report/omnichannel-fraud-report

 ©All Rights Reserved

Equifax Consumer Debt Observations

As of January 2024, the total US consumer debt is $17.33 trillion, up 2.3% over a year ago. Mortgage debt, including home equity loans, accounts for $12.58 trillion, a 72.6% share of total debt. Non-mortgage debt totals $4.75 trillion, equating to a 27.4% share.

In January 2024, 34.3% of non-mortgage consumer debt is from auto loans and leases, 31.9% is from student loans, and 23% is from credit card balances.

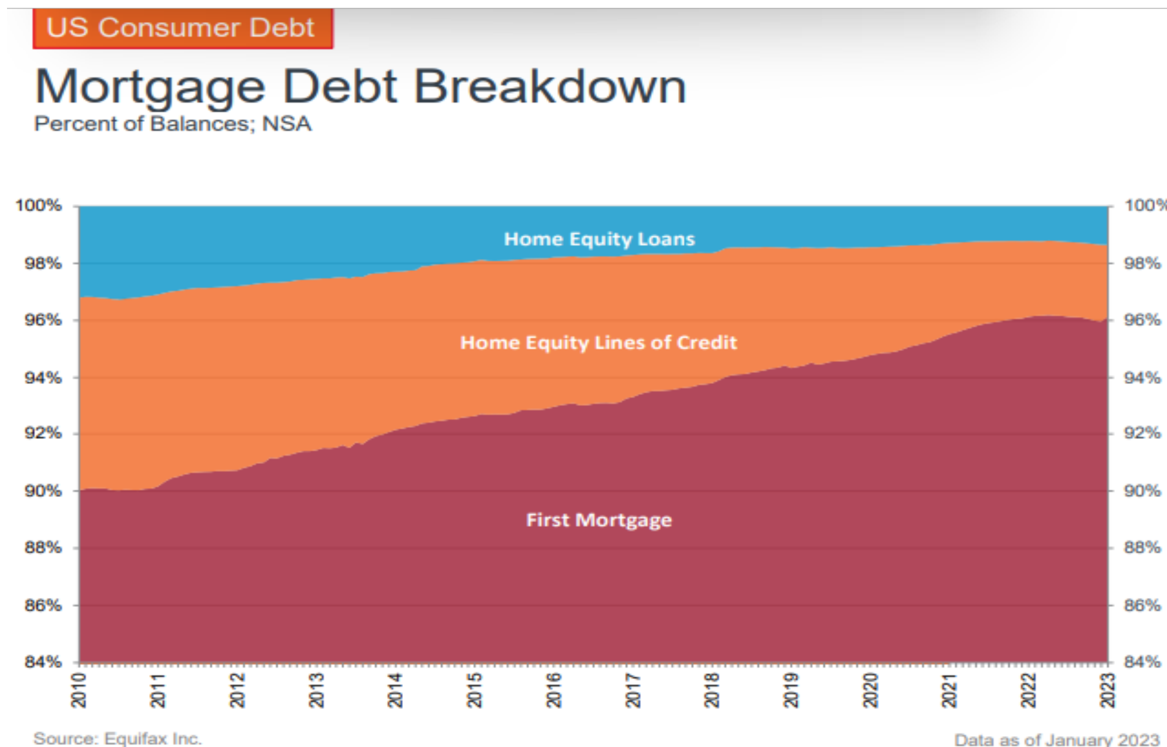
As of January 2024, HELOCs are 2.7% of mortgage debt outstanding and first mortgages account for 95.8%. Total mortgage debt is over 20% below the October 2008 peak level.

In January 2024, non-mortgage consumer debt write-offs came in at $12.98 billion, which is an increase of 41.8% over a year ago.

First Mortgage Trends

The following graph shows the growth of first mortgage debt for consumers over the last 20+ years.

[88]



[88] https://assets.equifax.com/marketing/US/assets/EFX_PortfolioCreditTrends_202301.pdf, page 11

 ©All Rights Reserved

First Mortgage Observation

As of January 2023, there were 53.28 million outstanding first mortgage loans, up 2.3% from January 2022.

First mortgage outstanding balances have risen steadily since June 2013 ($7.747 trillion), reaching $11.769 trillion.

The severe delinquency rate (share of balances 90+ Days Past Due, in bankruptcy or foreclosure) is 0.40%. This is up 7 bps from a year ago, when it stood at 0.33%.

Write-offs are at 0.48 bps on balances and 1.06 bps on accounts and are up from 0.38 bps and 0.77 bps from a year ago.

Home Equity Installment Loan Observations

Outstanding balances on home equity installment loans or fixed second mortgages rose 24.9% year-over-year to $166.0 billion.

The total number of outstanding home equity installment loans stands at 5.08 million, which is an increase of 13.1% compared to a year ago.

The severe delinquency rate (share of balances 90+ Days Past Due, in bankruptcy or foreclosure) is 0.73%, comparable with this time last year.

Monthly write-offs are at 14.06 bps as a share of outstanding balances.

This is 9.45 bps higher than the same time last year. HE Loan write-offs peaked in October 2008 at 38.8 bps.

Home Equity Lines of Credit Observations

Outstanding HELOC balances are $306.8 billion. This is a 2.2% increase in total balances from a year ago, and a 54.6% decrease from the May 2009 peak of $676.5 billion.

Outstanding HELOC accounts have similarly fallen over the past year from 7.95 million HELOCs in January 2022 to 8.99 million in January 2023, a 17.7% increase.

Utilization rates continue to trend down, sitting at 37.2% in January 2023 down from 37.3% a year ago. HELOC utilization rates peaked in December 2010 at 54.8%.

 ©All Rights Reserved

The severe delinquency rate (share of 90+ Days Past Due, in bankruptcy or foreclosure) is 0.44% which is a 10 bps decrease from the same month last year. In December 2009, severe delinquencies peaked at 2.86%.

Total aggregate HELOC credit limits continue to slowly trend down.

Senior Consumer Fraud

Seniors have long been targeted by fraudsters using the phone primarily to dupe seniors into sending money or other private information to savvy fraudsters. This segment of the population frequently are victims of violent crime, property crime, and consumer and telemarketing fraud. Scammers target those over fifty years of age with their telephone fraud schemes.

The Federal Trade Commission was authorized to enforce The Telemarketing and Consumer Fraud and Abuse Prevention Act, and target telephone fraud schemes to consumers.

The Act required the Federal Communications Commission (FCC) to promulgate regulations by -

1. defining and prohibiting deceptive telemarketing acts or practices
2. prohibiting telemarketers from engaging in a pattern of unsolicited telephone calls that a reasonable consumer would consider coercive or an invasion of privacy
3. restricting the hours of the day and night when unsolicited telephone calls may be made to consumers
4. requiring disclosure of the nature of the call at the start of an unsolicited call made to sell goods or services.[89]

Organizations including the Administration on Aging provide the elderly education about how to identify a scam, rules to never give out personal information over the phone, and updates on the current fraud scams affecting the elderly. Awareness is important for seniors to be aware of what scammers are doing and recognize when they are being scammed. They are also provided with the information to turn the fraudster in for legal action.

[89] https://www.ftc.gov/legal-library/browse/statutes/telemarketing-consumer-fraud-abuse-prevention-act

 ©All Rights Reserved

The Money Smart for Older Adults Program raises awareness among older adults and their caregivers on how to prevent fraud, scams, and other elder financial exploitation. The curriculum encourages advanced planning and informed financial decision-making.[90]

In the mortgage industry, reverse mortgage fraud has been a problem for seniors. A reverse mortgage is a special type of loan that allows homeowners 62 years of age and older to borrow against the accrued equity in their homes. The loan must be paid back when the borrower dies, moves, or no longer lives in the home. Fraud scams will get seniors to remove their property's equity only to get the funds stolen after loan funding.

For example - one fraud scam includes the homeowner's line of credit gets depleted shortly after closing often without the elderly homeowner's knowledge. Often this is done by an unethical family member, MLO, or fraudster.

Covid-19 pandemic has changed how people interact when managing financial matters with over the phone or electronic transactions, becoming the norm over face-to-face interaction. As a result of the economic uncertainty caused by the COVID-19 pandemic, scammers target older homeowners with home equity through reverse mortgage schemes.

These schemes can include:

- A trusted family member or caregiver coercing an elderly homeowner into applying for a reverse mortgage loan or impersonating their elderly relative during the loan process.
- Using an older homeowner's identity, Social Security number, or other personal information without his or her knowledge to get the equity loan money.
- Tempting reverse mortgage borrowers to use loan money to make a "can't miss" investment or to take out a reverse mortgage to pay for high-cost repairs or improvements to the home.
- Trying to convince the reverse mortgage borrower to sign a power of attorney that gives the scammer sole access to the reverse mortgage loan money.

[90] https://www.fdic.gov/resources/consumers/money-smart/teach-money-smart/money-smart-for-older-adults.html#:~:text=The%20Money%20Smart%20for%20Older,and%20informed%20financial%20decision%2Dmaking.

©All Rights Reserved

Many older homeowners do not realize they have been scammed until the loan money and their property equity is gone. Scammers may target older adults through community organizations; investment seminars; and television, radio, billboard, and mailer advertisements.[91]

The CFPB advises seniors that reverse mortgage ads do not always tell the whole story. They recommend they consider these facts when viewing an advertisement:

- A reverse mortgage is a home loan, not a government benefit. Reverse mortgages have fees and compounding interest that must be repaid, just like other home loans.
- A homeowner can lose their home with a reverse mortgage. **For example** - when a reverse mortgage ad says you will retain ownership of your home, or that you can live there as long as you want to, do not take these messages at face value.
- Without a good plan, a homeowner could outlive their loan money. **For example** - after seeing a reverse mortgage ad, a homeowner may think that a reverse mortgage guarantees financial security no matter how long you live.

Equity-rich, cash poor, elderly homeowners are an attractive target for unethical predatory lenders. Many elderly homeowners are on fixed or limited income yet need access to credit to pay for home repairs, medical care, property or municipal taxes, and other expenses. Predatory lenders profit from elders' needs for cash with loans packed with high interest rates, excessive fees and costs, credit insurance, balloon payments and other predatory terms.

Family Fraud Scams

When a family member cannot qualify, another family member will purchase the home in their name. The family member on the loan may not take occupancy of the property. Often, they will state they are going to rent their current home and move into the property they are purchasing. Yet after closing they allow the non-qualifying family member to move into the home, and they continue to occupy their existing home. There are some loan programs that would allow a non-occupying co-borrower to be on the loan and assist the borrower to qualify. Without disclosing the true occupancy of the property, this is considered occupancy fraud for housing.

---

[91] https://www.consumerfinance.gov/about-us/blog/avoid-reverse-mortgage-shopping-scams/

 ©All Rights Reserved

Additionally, a family member may try to steal the equity of another family member's home. The family member may steal the identity of the family member or push the transaction on the family member without explaining the transaction fully to the unsuspecting homeowner. Then the unethical family member may steal the cash equity with a second mortgage, reverse mortgage line of credit or cash out refinance. The homeowner may or may not be aware of the home loan transaction.

Air Loan Fraud Scheme

The air loan is a loan obtained on a nonexistent property or for a nonexistent borrower putting cash into the hands of the fraudsters. With no property ever bought or sold takes a group of professionals to work together to create a fake borrower, fake chain of title, and get a title and property insurance binder. The fraud chain may include phone banks and mailboxes to create fake employment verifications, home addresses and borrower telephone numbers.

Real Estate Cash Purchases Fraud

For this scheme, criminals use cash purchases to make payments in full for properties to evade the scrutiny on the origin of their funds they would experience by a financial institution. Many cash transactions are routine and legitimate, yet present significant opportunities for exploitation by unethical fraudsters.

Shell Companies Fraud

Criminals launder money to hide the illicit origin of their funds. Shell companies are typically non-publicly traded corporations, limited liability companies, or trusts that have no physical presence except a mailing address. Shell companies can be formed without disclosing the ultimate owners or people in control of them and can be used to conduct financial transactions without disclosing the true beneficial owners' involvement. Criminals abuse this anonymity to mask their identities, involvement in transactions, and origins of their wealth, hindering law enforcement efforts to identify individuals behind illicit activity.

Real Estate Broker Fraud

Real estate agents may be victims of a cash buyer scam that includes a fraudster that never intends to purchase the property. They lull a real estate agent to help them with cashier's check or bogus check and provide it to the broker. The fraudster identifies they have made an error in the amount or the account it was sent from and asks that all or a portion of the money be returned to them out of

 ©All Rights Reserved

the broker or escrow account. Unsuspecting, the broker sends the money only to find out the funds received were not legitimate when the cashier's check is processed.

Other Fraud Schemes

The increase in **income fraud** follows the trend of rising home prices with strong demand for homes. Most income fraud cases are fraud-for-housing motivated borrowers trying to qualify to purchase a home. Other income frauds are misrepresentations and may be fraud-for-profit schemes.

This typical fraud scenario includes the borrower having a new job with a significant pay increase or a high paying first job out of college. As it is a new job, the lender is unable to validate the job with the IRS.

Occupancy fraud occurs when mortgage applicants deliberately misrepresent their intended use for the property. Loan program pricing and guidelines change depending on the type of occupancy.

Transaction fraud occurs when the nature of the mortgage loan transaction is misrepresented. The risk includes third-party risk, non-arm length transactions and straw buyers. Straw buyers are often used when the fraudster has no intention of using or controlling the purchase of the home and disguises the true buyer or the true nature of the loan transaction.

Multi-closing fraud is a scam that takes advantage of the lag time between closing and recording showing in public record to obtain multiple loans on a single property. The fraudster will close several home loans simultaneously, often on the same day, allowing multiple liens on the property to provide cash out on each to the fraudster.

Identity Theft Fraud

The Red Flag Rules provision from amendments to the Fair Credit Reporting Act (FCRA) requires financial institutions to implement an identity theft prevention program. The Red Flag Rules requires a financial institution with consumers private information maintain policies and procedures for detecting, preventing, and mitigating identity theft.[92]

Identity theft is when one person uses another person's identity with illegal intensions. They may use someone's social security number or other personal information with illegal intensions for any number

[92] http://www.ftc.gov/bcp/edu/microsites/redflagsrule/diy-template.shtm

 ©All Rights Reserved

of illegal financial crimes, including opening new accounts, making purchases, buying a home, or getting someone's tax refund.

Mortgage loan originators are licensed professionals that are required to operate in a sound business manner that does not harm the consumer. Creditors require their staff to follow their company's comprehensive fraud and identity theft prevention program. While working with borrowers' mortgage loan originators must ensure who they are working with is in fact the person they presented to be. They must look for red flags that fall into five categories:

1. alerts, notifications, or warnings from a consumer reporting agency
2. suspicious documents
3. suspicious personally identifying information, such as a suspicious address (document information does not match credit report information)
4. unusual use of – or suspicious activity relating to – a covered account (such as checking account or credit card)
5. notices from customers, victims of identity theft, law enforcement authorities, or other businesses about possible identity theft in connection with covered accounts

When fraud is detected, the ethical procedure is to report the suspicious activity to a compliance or BSA officer. A mortgage loan originator is responsible to ensure they do not fund a fraudulent mortgage loan.[93]

ID Theft Prevention Program Compliance: A Four Step Process

The Red Flag Rules require mortgage lenders to have a comprehensive Fraud Prevention Program designed to identify and detect the warning signs (red flags) of identity theft in their day-to-day operations and prevent and mitigate identity theft from occurring. The Federal Trade Commission offers the following four step process for compliance.[94]

[93] https://www.finra.org/sites/default/files/Industry/p119095.pdf
[94] https://www.ftc.gov/tips-advice/business-center/guidance/fighting-identity-theft-red-flags-rule-how-guide-business

 ©All Rights Reserved

1. Identify Relevant Red Flags

The first step is to be able to identify and understand what the potential patterns, practices, or specific activities are indicating the possibility of identity theft.

Mortgage lenders must:

a. Understand the Risk Factors
    - Different types of accounts pose different kinds of risk. **For example** -a red flags for an owner-occupied home loan may differ from red flags for an investor home loan.
    - Consider other sources of information, including the other parties in the mortgage transaction. **For example** – is the transaction arms-length or do the parties have a previous relationship?
    - Technology and criminal techniques change constantly. Mortgage professionals must stay informed and up to date on new scams. **For example** – regulations require annual training to understand ethics and how to mitigate fraud.

b. Listen to the Red Flags, Alerts, Notifications, and Warnings from a Credit Reporting Company. Credit reports will flag information that is different from the last time the borrower had their credit pulled. Changes in a credit report or a consumer's credit activity might signal identity theft and requires the MLO to ask probing questions to identify if the person they are working with is the person they say they are. Some alerts could be:
    - a fraud or active-duty alert on a credit report
    - a notice of credit freeze in response to a request for a credit report
    - a notice of address discrepancy provided by a credit reporting company
    - a credit report indicating they work at different jobs or lines of work than what was provided on the loan application
        - **For example –** credit report shows borrower work for catering type companies, but the job on the application show he has worked in construction for ten years

c. Pay attention to Suspicious Documents. Reviewing the documents supplied by the borrower for red flags is an important part for MLOs. Loan document reg flags to look for include:
    - identification looks altered or forged
    - the person presenting the identification does not look like the photo, match the physical description, or wrong age
    - the bank statement columns look out of alignment

 ©All Rights Reserved

- fonts on the document vary and are not aligned

d. Look for Suspicious Personal Identifying Information. Personal identifying information can indicate identity theft inconsistencies with what is known.
   - information on the identification or application differs from information in borrower's credit file shows:
     - an address that does not match the credit report
     - the use of a Social Security number that is listed on the Social Security Administration Death Master File
     - a person who omits required information on an application and does not respond to notices that the application is incomplete

e. Review Notices from Other Sources. A customer, a victim of identity theft, a law enforcement authority, or someone else notifies the MLO that an account has been opened or identity used fraudulently.

2. Detect Red Flags

The Program must address the detection of red flags in connection with the opening of covered accounts and existing covered accounts. The mortgage lender's program must consider how the process can ensure the accuracy of the borrowers' identity and authentication methods that are effective. The method to obtain an identity verification or authentication will vary depending on if the loan application is taken in person, by telephone, mail, or online.

For online authentication, the Federal Financial Institutions Examination Council's guidance explores the application of multi-factor authentication techniques in high-risk environments, including using passwords, PINs, smart cards, tokens, and biometric identification. Certain types of personal information like a Social Security number, date of birth, mother's maiden name, or mailing address are not considered reliable authenticators because they are accessible online.[95]

3. Prevent and Mitigate Identity Theft

Once an MLO identifies a red flag, an MLO must be prepared to respond by following its company's policies and procedures in compliance with this regulation. Questionable activities or documents

---

[95] https://www.ffiec.gov/guidance/Authentication-and-Access-to-Financial-Institution-Services-and-Systems.pdf

©All Rights Reserved

should be escalated according to the degree of fraud suspected. When warranted, the MLO will need to complete a SAR (Suspicious Activity Report) to send to the BSA Officer or Compliance Officer in accordance with their company's policies. It is the MLOs responsibility to prevent fraud, and not fund fraudulent loans into the secondary market.

Funding a fraudulent loan is not worth losing your mortgage license or potential criminal record. Fraud costs the mortgage industry billions every year. If MLOs can help to prevent fraud, lenders would have better pricing and the home loan process would flow smoothly for the legitimate home loans. Fraud prevention is a team effort on all levels.

4. Update the Program

Mortgage companies spend a good portion of the budget on technology and protection of their software, facilities, and databases. As regulations and procedures change to stop fraud, fraudsters adapt and create new scams. A mortgage company must continually update and recognize new red flags as they emerge.

The Program must provide for the continued administration of the Program and must:

- Obtain approval of the initial written Program from either its board of directors or an appropriate committee of the board of directors. Fraud prevention comes from the top-down through a company.
- Involve the board of directors, an appropriate committee, or a designated employee at the level of senior management in the oversight, development, implementation, and administration of the Program.
- Train staff no less than annually to effectively implement the Program.

Customer Identification Program (CIP)

The Red Flag Rule contains guidance for what are considered "reasonable policies and procedures." A creditors program should contain procedures for verifying the customer's identity, starting with the identifying information obtained from the customer and non-documentary methods. These borrower

©All Rights Reserved

identification procedures should address customer verification through documents and third-party verifications.[96]

A CIP should specify acceptable personally identifying information that will be required of each customer applying for a covered account. At a minimum, this should include name, date of birth, address, and photo. The main government agencies require the borrower to provide a government issued photo ID (passport or driver's license) and copy of their social security card or other government tax identification.

For example - copy of a resident alien or individual taxpayer identification number (ITIN) card.

Additional verification for certain borrowers (for example, self-employed borrowers) who may need to document their liability and authority over the business.

Address Discrepancies Duties

The mortgage company's policies and procedures should be designed to train and enable an MLO or other employees who receives the notice of address discrepancy from a consumer reporting agency to take appropriate action to investigate the information discrepancy. The notice should indicate the address used to order the report given by the consumer differs from the address contained in the consumer report. Underwriters will require a satisfactory letter of explanation from the consumer.

The mortgage lender must document that an address is accurate by any of the following means:

1. Verification of the address with the consumer
2. Review of the organization's records
3. Verification of the address through third-party sources
4. Confirmation against other loan documents received and verified
5. Other reasonable means

If the mortgage lender cannot confirm the proposed borrower's information, this is a red flag and will require additional scrutiny of the information in the loan file and escalation to the BSA Officer in charge.

[96] https://www.consumerfinance.gov/rules-policy/regulations/1022/82/

©All Rights Reserved

Change of Address

According to the United States Postal Service (USPS), nearly 33.2 million addresses changes went through the post office in 2022.[97] In terms of identity theft, address fraud is one of the easiest crimes for criminals to perpetrate. The online ease to change your address opens the door for an exploitable weakness in the process.

USPS is very aware of address fraud and does what they can to prevent it from happening. Notably sending move validation letters to both the consumer's previous address and new address when they receive an address change request. USPS has changed to only accepting online address change requests with added layers of online fraud protection.

A criminal can do a lot of damage in a brief period of time. Some identity thieves have found a way to get around the USPS notice letter by putting a vacation hold on all mail to your current address.[98] This allows them even more time before you become aware of the identity theft crisis.

With FCRA regulations, the creditor is supposed to identify when a consumer is acting out of character and notice that the request for credit is not valid. Mortgage lenders have good reason to be concerned about the validity of address information.

Inconsistencies in the loan file are often a tip-off that the file contains misrepresentations, such as an address discrepancy warning on the credit report. The presence of one or more red flags in a file does not necessarily mean that there was fraudulent intent. However, several red flags in a file may signal a fraudulent transaction that will trigger additional scrutiny in providing this consumer with a mortgage or legal actions.

---

[97] https://facts.usps.com/total-address-changes/
[98] https://www.moving.com/tips/address-fraud-what-it-is-and-how-to-avoid-it/

 ©All Rights Reserved

Module 3 – Non-Traditional

Course Objective

In this lesson, the student will understand and learn about TILA Qualified Mortgage requirements as nontraditional loan programs may be termed non-qualified mortgages. Nontraditional loan programs reviewed in this course include a detailed review of adjustable-rate mortgages and how they function, and a review of commonly available renovation home loans. Students will understand the rehabilitation loan process and how to manage the different rehab loan requirements to help their consumers choose the program that meets their needs.

Traditional Mortgage Loan Defined

The Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act) defined what is considered a traditional loan as a 30-year fixed rate mortgage loan regardless of the type of occupancy or mortgage program investor. Any add-ons to the 30-year Note, such as balloon payments, rate adjustments, and interest-only payments will term a 30-year loan non-traditional.

For example - an owner-occupied 30-year fixed USDA home loan is considered traditional. An owner-occupied conforming 15-year fixed home loan would be considered a non-traditional.

TILA Qualified Mortgage

A non-Qualified Mortgage (non-QM) loan may be a 30-year fixed traditional mortgage loan, but because of certain risky loan features it would not be considered a qualified mortgage (QM). These TILA rules apply to owner-occupied properties requiring the lenders to verify the borrower is a qualified borrower and their loan program may not have any predatory lending features. These qualified mortgages must document the owner-occupied borrowers' ability to repay the debt, and in turn the creditor has some safe-harbor protections against potential fines and penalties for violating this regulation.[99]

A Qualified Mortgage is a category of loans that have certain, less risky features that help make it more likely the consumer will be able to afford their home loan. A lender must make a good-faith

---

[99] https://www.consumerfinance.gov/ask-cfpb/what-is-a-qualified-mortgage-en-1789/

 ©All Rights Reserved

effort to determine that all owner-occupied home loan applicants have the ability to repay their mortgage before the creditor closes the loan. This is known as the "ability-to-repay" rule. To be a Qualified Mortgage means the lender met specific requirements that include the ability-to-repay rule.[100]

Generally, the requirements for a qualified mortgage rule include:

- No risky loan features are permitted, such as:
  - An "interest-only" period, when they pay only the interest due without paying down the principal, which does not decrease the amount of money they borrowed.
  - "Negative amortization," which can allow their loan principal to increase over time, because they are making less than interest accruing on the loan.
  - "Balloon payments," which are bulk amount payments at the end of a loan term or specific period of time in the loan repayment.
  - Loan terms that are longer than 30 years.
- Limits on the price of a loan. The annual percentage rate, or APR, on a Qualified Mortgage cannot be higher than a specified threshold. These thresholds are posted annually in the federal register.
- No excess upfront points and fees. Thresholds are used to determine when fees are excessive. Not all loan fees are included in the threshold. **For example** - FHA insurance premiums are included in this limit. If the points and fees exceed the threshold, then the loan cannot be considered a Qualified Mortgage.
- Diligently verify income, assets, and debts. A Qualified Mortgage must consider and verify the qualifying income and assets to determine the borrower can manage their monthly obligation at loan closing. This requires lenders to include any proposed or known additional debts the borrower will have even after closing. All debts must be included to determine the total debt-to-income ratio. In addition, the creditor should review the money a borrower has left after paying all their monthly debts, known as residual income, to ensure the borrower can repay the Qualified Mortgage.[101]

[100] https://www.consumerfinance.gov/rules-policy/regulations/1026/43/#e-2
[101] https://www.consumerfinance.gov/ask-cfpb/what-is-a-qualified-mortgage-en-1789/

 ©All Rights Reserved

Qualified Mortgage Thresholds

For qualified mortgages (QMs), the thresholds for the spread between the annual percentage rate (APR) and the average prime offer rate (APOR) change annually. In 2024 they will be as follows:

- 2.25 or more percentage points for a first lien covered transaction with a loan amount greater than or equal to $130,461
- 3.5 or more percentage points for a first lien covered transaction with a loan amount greater than or equal to $78,277 but less than $130,461
- 6.5 or more percentage points for a first lien covered transaction with a loan amount less than $78,377
- 6.5 or more percentage points for a first lien covered transaction secured by a manufactured home with a loan amount less than $130,461
- 3.5 or more percentage points for a subordinate-lien covered transaction with a loan amount greater than or equal to $78,277; or
- 6.5 or more percentage points for a subordinate-lien covered transaction with a loan amount less than $78,277.

For all categories of QMs, the thresholds for total points and fees as of the writing of this course:

- Three percent of the total loan amount for a loan greater than or equal to $130,461
- $3,914 for a loan amount greater than or equal to $78,277 but less than $130,461
- Five percent of the total loan amount for a loan greater than or equal to $26,092 but less than $78,277
- $1,305 for a loan amount greater than or equal to $16,308 but less than $26,092; and
- Eight percent of the total loan amount for a loan amount less than $16,308.[102]

Ability to Repay

The Dodd-Frank Act required lenders to make a reasonable, good-faith determination of a consumer's ability to repay (ATR) any mortgage home loan secured by their owner-occupied dwelling (excluding an open-end credit plan, timeshare plan, reverse mortgage, or temporary loan), and establishes

[102] https://www.federalregister.gov/documents/2023/09/21/2023-20476/truth-in-lending-regulation-z-annual-threshold-adjustments-credit-cards-hoepa-and-qualified

 ©All Rights Reserved

certain safe harbor protections for creditors from liability under this requirement for Qualified Mortgages (QM).

The ATR rule applies to all owner-occupied QM loans regardless of the loan terms or funding investor. The ATR/QM rule requires lenders to retain evidence of compliance with the rule for three years after a covered loan is consummated.

To rebut the presumption of compliance, it must be proven that, despite meeting the prerequisites in the regulations, the creditor did not make a reasonable and good faith determination of the consumer's repayment ability at the time of consummation. The lender may disprove this by showing that the consumer's income, debt obligations, alimony, child support, and the consumer's monthly payment (including mortgage-related obligations) on the covered transaction and on any simultaneous loans the creditor was aware at consummation would leave the consumer with sufficient residual income or assets. The lender must properly document how it made the assumption the borrower would be able to meet living expenses, including any recurring and material non-debt obligations of which the creditor was aware at the time of consummation.[103]

Exempt From Ability-to-repay Rule

According to the regulations, a few special types of lenders are exempt from the ability-to-repay rule. Lenders and programs that may not have to follow the ability-to-repay rules are:

- Community Development Financial Institutions. These groups are certified by the U.S. Department of the Treasury to provide credit and financial services to underserved populations. The Department of the Treasury has more information on Community Development Financial Institutions.
- Community Housing Development Organizations or Down payment Assistance Providers of Secondary Financing. These are nonprofit service groups that receive aid from the Department of Housing and Urban Development (HUD) to help provide affordable housing in their communities.

[103] https://www.consumerfinance.gov/rules-policy/regulations/1026/43/#e-1-ii-B

©All Rights Reserved

- Nonprofit organizations that lend less than two hundred times a year and provide credit only to low- or moderate-income consumers. These groups must follow their own written procedures to determine that consumers have a reasonable ability to repay their loans.
- Housing Finance Agencies, which are state agencies that offer certain mortgages with low rates for low- and moderate-income borrowers.
- Loans made through programs under the Emergency Economic Stabilization Act. These programs help those communities hardest hit by the financial crisis of 2007 and 2008.[104]

Alternative Mortgage Transactions According to Regulation D

Alternative mortgage transaction means a loan, credit sale, or account:

1. That is secured by an interest in a residential structure that contains one to four units, whether or not that structure is attached to real property, including an individual condominium unit, cooperative unit, mobile home, or trailer, if it is used as a residence.
2. That is made primarily for personal, family, or household purposes; and
3. In which the interest rate or finance charge may be adjusted or renegotiated.

Regulation D was issued by the Bureau of Consumer Financial Protection (CFPB) to implement the Alternative Mortgage Transaction Parity Act as amended and the Truth in Lending Act.[105] Consistent with the Alternative Mortgage Transaction Parity Act, the Truth in Lending Act, and the Dodd-Frank Wall Street Reform and Consumer Protection Act, the purpose of this regulation is to balance access to responsible credit and enhanced parity between State and federal housing creditors regarding the making, purchase, and enforcement of alternative mortgage transactions with consumer protection and the interests of the States in regulating mortgage transactions generally.

Alternative mortgage transaction that includes any consumer credit transaction secured by a mortgage, deed of trust, or other equivalent consensual security interest in a dwelling or in residential real property that includes a dwelling. The dwelling need not be the primary dwelling of

[104] https://www.consumerfinance.gov/ask-cfpb/my-mortgage-lender-told-me-it-was-exempt-from-the-ability-to-repay-mortgage-rule-is-this-true-en-1793/

[105] Alternative Mortgage Transaction Parity Act, 12 U.S.C. §3801 et seq.

 ©All Rights Reserved

the consumer. Home equity lines of credit and subordinate lien mortgages are alternative mortgage transactions for purposes of this regulation.[106]

Examples of alternative mortgage transactions include:

- Transactions in which the interest rate changes in accordance with fluctuations in an index.
- Transactions in which the interest rate or finance charge may be increased or decreased after a specified period of time or under specified circumstances.
- Balloon transactions in which payments are based on an amortization schedule and a large final payment is due after a shorter term than the amortization. The creditor makes a commitment to renew the transaction at specified intervals throughout the amortization period, but the interest rate may be renegotiated at renewal. **For example** - a fixed-rate mortgage loan with a 30-year amortization period but it has a balloon payment due five years after consummation is an alternative mortgage transaction if the creditor commits to renew the mortgage at five-year intervals for the entire 30-year amortization period.
- Transactions in which the creditor and the consumer agree to share some or all of the appreciation in the value of the property (shared equity/shared appreciation).

The following are examples of transactions that are not alternative mortgage transactions:

- Transactions with a fixed interest rate where one or more of the regular periodic payments may be applied solely to accrued interest and not to loan principal (an interest-only feature).
- Balloon transactions with a fixed interest rate where payments are based on an amortization schedule and a large final payment is due after a shorter term, where the creditor does not make a commitment to renew the transaction at specified intervals throughout the amortization period.
- Transactions with a fixed interest rate where one or more of the regular periodic payments may result in an increase in the principal balance (a negative amortization feature).[107]

A creditor that makes an alternative mortgage transaction with an adjustable rate or finance charge may only increase the interest rate or finance charge as follows:

---

[106] https://www.consumerfinance.gov/rules-policy/regulations/1004/2/#2-a-Interp-3-ii
[107] https://www.consumerfinance.gov/rules-policy/regulations/1004/2/#c-3

 ©All Rights Reserved

- The creditor must comply with the general TILA disclosure requirements
- For all other transactions, the creditor must use either:
    - An index to which changes in the interest rate are tied that is readily available to and verifiable by the borrower and beyond the control of the creditor; or
    - A formula or schedule identifying the amount that the interest rate or finance charge may increase and the times at which, or circumstances under which, a change may be made.[108]

A creditor may use any measure of index values that meets the requirements in the regulations**. For example** - the index may be either single values as of a specific date or an average of values calculated over a specified period.

A creditor may increase an adjustable interest rate only if the increase is based on an index that is beyond the creditor's control. An index is not beyond the creditor's control if the index is the creditor's own prime rate or cost of funds. A creditor is permitted, however, to use a published prime rate, such as the prime rate published in the Wall Street Journal, even if the creditor's own prime rate is one of several rates used to establish the published rate.[109]

The index must be available to the public. A publicly available index need not be published in a newspaper, but it must be one the consumer can independently obtain **(for example** - by telephone) and use to verify the annual percentage rate applied to the alternative mortgage transaction.

Mortgages With Adjustable or Renegotiable Rates or Finance Charges

A creditor that makes an alternative mortgage transaction with payments based on an amortization period and a large final payment due after a shorter term may negotiate an increase or decrease in the interest rate when the transaction is renewed only if the creditor makes a written commitment to renew the transaction at specified intervals throughout the amortization period. However, the creditor is not required to renew the transaction if:

- Any action or inaction by the consumer materially and adversely affects the creditor's security for the transaction or any right of the creditor in such security

---

[108108] https://www.consumerfinance.gov/rules-policy/regulations/1004/4/#de38a82277268f404065254dafd5d4914192d0c3b36d54d4642f206f
[109] § 1004.4(a)(2)(i)

 ©All Rights Reserved

- There is a material failure by the consumer to meet the repayment terms of the transaction
- There is fraud or a willful or knowing material misrepresentation by the consumer in connection with the transaction
- Federal law dealing with credit extended by a depository institution to its executive officers specifically requires that as a condition of the extension the credit shall become due and payable on demand, provided that the creditor includes such a provision in the initial agreement.[110]

State Law Restrictions

State laws may put restrictions on the adjustment or renegotiation of an interest rate or finance charge, including restrictions on the circumstances under which a rate or charge may be adjusted, the method by which a rate or charge may be adjusted, and the amount of the adjustment to the rate or charge.

For example - if a provision of State law prohibits creditors from increasing an adjustable rate more than two percentage points or from increasing an adjustable rate more than once during a year, that provision is preempted with respect to alternative mortgage transactions that comply. Similarly, if a provision of State law prohibits housing creditors from renewing balloon transactions that meet the definition of an alternative mortgage transaction on different terms, that provision is preempted only to the extent that it restricts a state housing creditor's ability to adjust or renegotiate the interest rate or finance charge at renewal.

State laws may restrict the ability of a housing creditor to change the amount of interest or finance charges included in regular periodic payments as a result of the adjustment or renegotiation of an interest rate or finance charge.

For example - if a provision of State law prohibits housing creditors from increasing payments or limits the amount of such increases with respect to both alternative mortgage transactions and other mortgage transactions, to the extent that it restricts a housing creditor's ability to adjust payments because of the adjustment or renegotiation of an interest rate. Other restrictions on changes to payments are not preempted, including restrictions on transactions in which one or more of the

---

[110] https://www.consumerfinance.gov/rules-policy/regulations/1004/4/#7ae2562961d72df6ca35db9818a90553ee87215eec5e8e9b1b9521e1

 ©All Rights Reserved

regular periodic payments may result in an increase in the principal balance (a negative amortization feature) or may be applied solely to accrued interest and not to loan principal (an interest-only feature).

State regulations may have restrictions on the creditor and the consumer sharing some or all of the appreciation in the value of the property (shared equity/shared appreciation).

Preempted State Laws

The following are examples of State laws that are not preempted regardless of whether the provision applies solely to alternative mortgage transactions or to both alternative mortgage transactions and other mortgage or consumer credit transactions:

- Restrictions on prepayment penalties or late charges (including an increase in an interest rate or finance charge as a result of a late payment).
- Restrictions on transactions in which one or more of the regular periodic payments may result in an increase in the principal balance (a negative amortization feature) or may be applied solely to accrued interest and not to loan principal (an interest-only feature).
- Requirements that disclosures be provided.[111]

Adjustable-Rate Mortgage

An adjustable-rate mortgage (ARM) allows lenders the ability to increase their profits more so than a fixed rate home loan. Adjustable rates change over the entire life of a loan as indexes adjust, according to the terms in the note, to reflect the current cost of money. Many lenders like ARMs because they can pass the risk of fluctuating interest rates onto the borrowers. Lenders may offer multiple types of ARM programs.

Sometimes it does not make sense to take an adjustable-rate mortgage, but that is short sited.

For example - If you have a borrower that plans to pay their principal down rapidly or with a large lump sum inheritance, an ARM could be a benefit. If you have a consumer making a large lump sum or extra loan payments because they want an overall lower payment, an ARM loan would work the

[111] https://www.consumerfinance.gov/rules-policy/regulations/1004/interp-3/

 ©All Rights Reserved

best for this consumer. The monthly payment would go down when the loan adjusts because the principal is less. The loan will amortize with the lower outstanding balance with every adjustment.

With a fixed rate loan, the payment will never change even if the mortgage balance changes drastically, although it would pay off sooner than 360 payments.

Terms, rate changes, and many other aspects of ARMs are regulated primarily by TILA disclosure requirements. Any ARM guidelines of Fannie Mae, Freddie Mac, FHA, and private mortgage insurers must be followed as well.

Components of an ARM Loan

There are several parts to an ARM:

- Index
- Margin
- Rate adjustment period
- Interest rate cap
- Floor rate
- Conversion option (if applicable)

Index

For an adjustable-rate mortgage, the index is a benchmark interest rate that reflects general market conditions, and the margin is a number set by the lender when the borrower applies for a home loan.

With an adjustable-rate mortgage, the rate stays the same, generally for the first year or a few years, and then it begins to adjust periodically. Once the rate begins to adjust, the changes to the interest rate are based on the market index, not on the borrowers' personal financial situation.

Once the initial interest rate for the loan is set at the time of rate lock. The interest rate for the loan is tied to a widely recognized and published index. The index is often referred to as the cost of money.

 ©All Rights Reserved

Changes in the index, along with the loan's set margin, determine the changes to the interest rate for an adjustable-rate mortgage loan. The lender decides which index your loan will use when you apply for the loan, and this choice will not change after closing.[112]

Common ARM mortgage indices include:

COFI - A monthly cost-of-funds index (COFI) reflecting the weighted-average interest rate paid by 11th Federal Home Loan Bank District savings institutions for savings and checking accounts. The 11th district covers Arizona, California, and Nevada. The Federal Cost of Funds Index (COFI) is used as a benchmark for some types of mortgage loans and securities. It is calculated as the sum of the monthly average interest rates for marketable Treasury bills and for marketable Treasury notes, divided by two, and rounded to three decimal places.[113]

The Federal COFI is made available by Freddie Mac on or about the 20th day of each month. Freddie Mac first began publicly providing the Federal COFI in March 1991. The Federal COFI is not adjusted to reflect subsequent changes in the underlying Treasury rates once the value has been posted.

CMT – Constant Maturity Treasury is an index published by the Federal Reserve Board based on the monthly average yield of a range of Treasury securities, all adjusted to the equivalent of a one-year maturity. Yields on Treasury securities at constant maturity are determined by the U.S. Treasury from the daily yield curve. CMT is less volatile than the daily 11th District Cost of Funds and is used for many ARM loan programs.[114]

SOFR - The Secured Overnight Financing Rate (SOFR) is based on actual transactions in the Treasury repurchase (repo) market, where extensive trading happens daily. This is the market where investors offer borrowers overnight loans backed by their U.S. Treasury bond assets.[115]

---

[112] https://www.consumerfinance.gov/ask-cfpb/for-an-adjustable-rate-mortgage-arm-what-are-the-index-and-margin-and-how-do-they-work-en-1949/

[113] https://www.google.com/search?q=11th+district+cost+of+funds+index&rlz=1C1CHZN_enUS1022US1022&oq=11th+district+cost+of+funds+index&gs_lcrp=EgZjaHJvbWUyCQgAEEUYORiABDIHCAEQABiABDIICAIQABgWGB4yDQgDEAAYhgMYgAQYigXSAQg2MzUwajBqNKgCALACAQ&sourceid=chrome&ie=UTF-8

[114114] https://www.bankrate.com/rates/interest-rates/1-year-cmt/

[115] https://sf.freddiemac.com/working-with-us/origination-underwriting/mortgage-products/sofr-indexed-arms#:~:text=The%20Secured%20Overnight%20Financing%20Rate,their%20U.S.%20Treasury%20bond%20assets.

 ©All Rights Reserved

Each business day, the New York Fed publishes the SOFR on the New York Fed website at approximately 8:00 a.m. ET.[116] Lenders use the 30-day average SOFR to price mortgage loan programs. This is the index that replaced the previously popular LIBOR index.

Prime Rate Index – The prime rate is the underlying index for most credit cards, home equity loans and lines of credit, auto loans, and personal loans. Many small business loans are also indexed to the Prime rate.

The Prime Rate is consistent because banks want to offer businesses and consumers loan products that are both profitable and competitive. Most home equity lines of credit will use the Prime Rate Index + margin to determine the rates offered.[117]

Margin

The margin is the number of percentage points added to the index to set the interest rate on an adjustable-rate mortgage (ARM) after the initial rate period ends. The margin is set when the loan is locked and included in the ARM loan agreement that cannot change after closing. The margin amount depends on the particular lender, costs paid at closing and type of loan.[118] The lower the margin generally the higher the start rate, because the lower the margin the less the rate adjustment changes.

The margin added to the index is termed the fully indexed rate.

For Example -

5.33%	Current SOFR Index Value as of 3/30/2024
+ 2.00%	Margin
7.33%	Fully Indexed Rate will be rounded down to the nearest 1/8th. 7.325%

Rate Adjustment Period

The rate adjustment period is the length of time between interest rate changes with ARMs. This period can vary depending on the terms in the Note.

---

[116] https://www.newyorkfed.org/markets/reference-rates/sofr
[117] http://www.fedprimerate.com/
[118] https://www.consumerfinance.gov/ask-cfpb/for-an-adjustable-rate-mortgage-arm-what-are-the-index-and-margin-and-how-do-they-work-en-1949/

©All Rights Reserved

Discounted Rates

When the initial rate on an ARM, or start rate, is less than the current fully indexed rate, the ARM rate is considered a discounted rate. The discounted rate ('Teaser Rate') can make the ARM loans more attractive to consumers who have a short-term period before moving or refinancing and will benefit with a lower monthly payment.

Interest Rate Cap

Interest rate caps are used with ARMs to limit the percentage points interest rate may increase during the adjustment period and life of the loan. Caps limit on interest rate and payment increase to prevent large fluctuations in mortgage payments and payment shock for borrowers.

Rate caps are often shown as two numbers, for example, 2/6

- 2/6 – The first number – 2 - indicates the maximum amount the interest rate can increase or potentially decrease from one adjustment period to the next. Provided the rate does not go lower than the allowable floor rate.
- 2/6 – The second number – 6 - indicates the maximum amount the interest rate can increase during the life of the loan. At the 6% cap, no additional increase can be made in the rate. The rate can go down as the market allows, but never higher than the life of loan cap allows.

Some ARMs allow for a higher rate adjustment for the first adjustment, especially with hybrid ARM programs. After the first adjustment, then a lower subsequent adjustment cap applies to future adjustments. These ARMs are usually identified with three numbers, where the first number is the interest rate cap for the first adjustment period, the second number is the subsequent adjustment cap, and the third number is the lifetime interest rate cap.

For example - if you see a rate cap described as 3/2/6, the interest rate cannot increase more than:

- 3% at the first adjustment period
- 2% for subsequent adjustment periods through the life of the loan
- 6% total over the life of the loan

Floor Rate – the minimum an ARM loan may adjust down over the life of the loan. Many ARM loans use the start rate as the floor rate.

©All Rights Reserved

ARM Functions

When attempting to understand how an ARM loan works and how payments adjust, think of an ARM as a set of steps. The floor (bottom of the steps), where the ARM rate begins, is the initial rate's period of time from closing until the first adjustment period – start rate, initial rate, or teaser rate. The next number is the subsequent adjustments of the entire term of the loan, but the ARM interest rate may never exceed the start rate plus the life of loan cap.

For example - 1 year ARM loan closes with 6% start rate, 3% margin and 2/6 adjustment caps. At the first adjustment one year later, with the SOFR index at 5.375%, what will the interest rate be at time of adjustment and how long will the rate be effective?

1. The first calculation is to identify the fully indexed rate. The max rate may increase based on the index. The first adjustment after one year may be the current index + the margin = fully indexed rate. (5.375% SOFR index + 3% margin = 8.375% Fully index rate)
2. The second calculation uses the caps to identify the maximum adjustment allowed. Start rate plus the first adjustment cap. (6% start rate + 2% first & subsequent cap = 8% maximum interest rate increase for first adjustment)
3. The lesser of the fully indexed rate or the maximum interest rate cap for the adjustment sets the interest rate for the coming year. In this case the first adjustment cap kept the interest rate from increasing to the fully indexed rate.
4. For this first adjustment, the borrower's rate for the 13th through 24th month repayments will be based on amortization of 8.00%.

Use the same method for next year's interest rate adjustment. With the "stairs" method, the 1-year ARM loan coming up on a subsequent adjustment is currently at 8%. The margin is the same at 3% and adjustment caps are 2/6. For the subsequent adjustment on the second year after closing, and one year from last adjustment this is the process. We estimate the SOFR is 4.75%. Calculate the second subsequent adjustment as follows:

1. The fully indexed rate. The subsequent adjustment after one year would be the current index + the margin = fully indexed rate. (4.75% SOFR index + 3% margin = 7.75% Fully index rate)
2. The second calculation uses the caps to identify the maximum adjustment allowed. Current interest rate plus the subsequent adjustment cap. (8.00% start rate + 2% subsequent cap = 10.00% maximum interest rate for this adjustment).

 ©All Rights Reserved

3. The lesser of the fully indexed rate or the maximum interest rate sets the interest rate for the coming year. In this scenario, the fully indexed rate is the lowest calculation.
4. For this adjustment, the borrower's rate for the 25th through 32nd month repayments will be based on amortization of 7.75%.
5. As previously stated, the loan's interest rate may never exceed the lifetime cap. Start rate + lifetime cap = highest interest rate capped.
    a. For this scenario, 6% start rate + 6% life of loan cap = 12% max the interest rate may ever be in this scenario.

Hybrid ARM

A hybrid ARM is an ARM with an initial fixed-rate period greater than one year. That is, the loan has a fixed rate for a specific number of years, and then the interest rate adjusts regularly for the remaining term of the loan. The adjustments are set by the terms in the Note.

For example - A 3/1 hybrid ARM has an introductory rate period or teaser rate for the first three years after closing. Other longer period options include 5/1, 7/1, or 10/1 ARMs, where the fixed period is for five, seven, or ten years and the interest rate adjust annually for the remainder of the loan term.

For hybrid loans, often the longer the initial period of stable payments, the higher the first adjustment cap. The caps for a 5/1 hybrid ARM are generally 3/2/6. With this configuration, the first number is the first adjustment cap, the second is the subsequent adjustment cap and the last is the lifetime cap.

For example - 3/1 year ARM loan closes with 7.5% start rate, 2.50% margin and 3/2/6 adjustment caps. At the first adjustment three years later, with the SOFR index at 5.125%, what will the interest rate be at time of adjustment?

1. The first calculation is to identify the fully indexed rate. The max the interest rate may increase based on the index. The first adjustment after three years would be the current index + the margin = fully indexed rate. (5.125% SOFR index + 2.50% margin = 7.625% Fully index rate)
2. The second calculation uses the caps to identify the maximum adjustment allowed. Start rate plus the first adjustment cap. (7.50% start rate + 3% first cap = 10.50% maximum interest rate for first adjustment)

©All Rights Reserved

3. The lesser of the fully indexed rate or the maximum interest rate sets the interest rate for the coming year. For this first adjustment, the borrower's rate for the 37th through 49th month payments will be based on amortization of 7.625% interest rate.

After the initial interest rate adjustment, the 3/2/6 caps would use the 2% for subsequent adjustment caps with the lifetime 6% cap setting the maximum interest rate allowed.

Negative Amortization Loans

Negative amortization occurs anytime the monthly payment is not sufficient to cover the accrued interest from the previous month. For negative amortization, the borrower will pay a smaller percent of interest due, than what the loan is accruing interest at.

For example - if the fully indexed interest rate being charged by the lender is 7% and the borrower is paying 5% interest payments every month as their option ARM payment, the 2% of interest not being paid every month will be added to the principal balance each month. This causes the cost of the money to increase monthly as the outstanding loan balance increases.

According to CFPB interpretations, amortization means paying off a loan with regular payments, so that the amount you owe goes down with each payment. Negative amortization means that even when you pay, the amount you owe will still go up because you are not paying enough to cover the interest. These loans require added disclosure statements.

For example - The disclosure might state, "If any of your payments are not sufficient to cover the interest due, the difference will be added to your loan amount." Loans that provide for more than one way to trigger negative amortization are separate variable-rate programs requiring separate disclosures.

If a consumer is given the option to cap monthly payments that may result in negative amortization, the creditor must fully disclose the rules relating to the option, including the effects of exercising the option (such as negative amortization will occur and the principal loan balance will increase), however, the variable rate disclosure need not be provided.

Consumers are advised to pay the interest due at a minimum to avoid negative amortization. Paying the interest only provides the principal balance does not increase, but also the loan balance does not decrease like a fully amortized payment loan would do.

©All Rights Reserved

These types of loans were popular in the early 2000's, but after the market crash of 2007 and subsequent changes in federal laws, these loans have limited offerings except for risk layered investor loan programs.

Conversion Option

Some ARM loan programs may allow the borrower to convert the adjustable-rate mortgage into a fixed rate mortgage without the expense of a refinance or re-qualifying for a new loan if the original Note allows for this conversion. The Note will provide a window of time called the conversion period, and the borrower must exercise their option to convert the adjustable-rate mortgage to a fixed rate mortgage during this specific conversion period. Once this period has ended, the loan will remain an ARM loan until paid in full.

According to CFPB interpretations, if a loan program permits consumers to convert their variable-rate loans to fixed-rate loans, the lender must disclose that the interest rate may increase if the consumer converts the loan to a fixed-rate loan. The lender must also disclose the rules relating to the conversion feature, such as the period during which the loan may be converted, that fees may be charged at conversion, and how the fixed rate will be determined.

The lender should identify any index or other measure, or formula used to determine the fixed rate and state any margin to be added. In disclosing the period during which the loan may be converted and the margin, the lender may use information applicable to the conversion feature during the six months preceding preparation of the disclosures and state that the information is representative of conversion features recently offered by the lender.

Consumer Handbook on Adjustable-Rate Mortgages

The Consumer Handbook on Adjustable-Rate Mortgages (CHARM Booklet) is a TILA requirement for all home loans with an adjustable-rate mortgage loan. The CHARM Booklet is provided with the application disclosures and Loan Estimate.[119] The CHARM booklet explains the functions of the ARM loan program.

---

[119] https://files.consumerfinance.gov/f/documents/cfpb_charm_booklet.pdf

©All Rights Reserved

Loan Estimate for ARM Loan

When an MLO is offering an ARM loan there are more loan terms that need to be disclosed on the Loan Estimate. The following is an example of the Loan Term section provided by CFPB as an example. The Loan Terms section is on page one of the Loan Estimate.

Loan Terms		Can this amount increase after closing?	
Loan Amount	$216,000	**NO**	
Interest Rate	3%	**YES**	· Adjusts **every year** starting in year 6 · Can go **as high as 8%** in year 8 · See **AIR Table** for details
Monthly Principal & Interest *See Projected Payments Below for Your Total Monthly Payment*	$910.66	**YES**	· Adjusts **every year** starting in year 6 · Can go **as high as $1,467** in year 8
		Does the loan have these features?	
Prepayment Penalty		**NO**	
Balloon Payment		**NO**	

Projected payments show the borrower a worst-case scenario over the life of the loan. Found on page 1 of Loan Estimate.

Projected Payments				
Payment Calculation	**Years 1-5**	**Years 6**	**Years 7**	**Years 8-30**
Principal & Interest	$910.66	$838 min $1,123 max	$838 min $1,350 max	$838 min $1,467 max
Mortgage Insurance	+ 99	+ 99	+ 99	+ —
Estimated Escrow *Amount can increase over time*	+ 341	+ 341	+ 341	+ 341
Estimated Total Monthly Payment	$1,290	$1,217 – $1,502	$1,217 – $1,729	$1,179 – $1,808
Estimated Taxes, Insurance & Assessments *Amount can increase over time*	$341 a month	**This estimate includes** ☒ Property Taxes ☒ Homeowner's Insurance ☐ Other: *See Section G on page 2 for escrowed property costs. You must pay for other property costs separately.*		**In escrow?** **YES** **YES**

Adjustable Interest Rate (AIR) table section gives the details of the ARM loan terms. Found on page two of the Loan estimate.[120]

[120] https://files.consumerfinance.gov/f/documents/cfpb_charm_booklet.pdf

 ©All Rights Reserved

Adjustable Interest Rate (AIR) Table	
Index + Margin	1 Year Cmt + 2.5%
Initial Interest Rate	3%
Minimum/Maximum Interest Rate	2.5% / 8%
Change Frequency	
First Change	Beginning of 61st month
Subsequent Changes	Every 12 months after first change
Limits on Interest Rate Changes	
First Change	2%
Subsequent Changes	2%

Collateral/Portfolio Loans

Commercial 'hard money,' portfolio lenders, or collateral lenders have been around since the first borrower used their homestead as collateral for a loan. Portfolio lending allows the individual with the money (investor) to determine the guidelines for the loan risk they are willing to take given the borrower's credit worthiness and property soundness to support the evaluation. The investor may then set the interest rate they will accept for the file risk. There are state usuary laws that can limit some loans depending, but many hard money lenders are reasonable as they want repeat business and referrals along with their high rates of return.

Private money lenders are mortgage brokers that will lend their own personal funds, or pooled investors funds. These investors set their guidelines and will ask for high-interest rates and points charged at closing to ensure their return on investment is worth funding the borrower's loan. These types of loans are not sellable on the normal secondary mortgage market but are retained and serviced by the funding investor.

Private money is generally a short-term loan and fixes a borrower's current need or issue. It is important MLOs provide the borrower with an exit plan to pay off the high-rate private money loan in the future and obtain a more affordable conforming home loan.

Seller Financing

Seller Financing is similar but should not be confused with collateral lending. Seller financing is an individual with sufficient equity in their property that they want to defer the tax burden or earn interest on the equity they use to lend to the purchaser.

Not all mortgage loan programs will allow seller financing. Check your guidelines for LTV and CLTV limits.

©All Rights Reserved

The use of scam seller financing has been used as a fraud scheme for decades. The seller forgives the seller financing or second mortgage after closing because the property was never worth the purchase price. The creditor is then sitting with a 100%+ LTV loan in their portfolio. Any home loan requests with seller financing will have extra scrutiny to ensure the transaction is arms-length.

Rehabilitation Loans

Eligible Property Types

- Single family homes
- Single family homes with eligible accessory dwelling units (ADUs)
- Two-to-four family units
- Townhomes
- Manufactured homes titled as real estate, where the rehabilitation does not affect the structural components
- Eligible condominium units and site condo units (improvements are limited to the unit's interior)
- HUD Homes/Real-Estate Owned properties (no additional FHA appraisal required with FHA home financing)
- Mixed use properties that are primarily residential (at least 51%)

FHA 203(k) Rehabilitation Mortgage Insurance Program

Section 203(k) insures mortgages covering the purchase or refinancing and rehabilitation of a home that is at least a year old. A portion of the loan proceeds are used to pay the seller, or if a refinance, to pay off the existing mortgage. The remaining funds are placed in an escrow account and released when the rehabilitation is completed.

Section 203(k) offers:

- a solution that helps both borrowers and lenders, insuring a single, long term, fixed or adjustable-rate loan that covers the acquisition and rehabilitation of a property.
- affordability and flexibility of FHA-insured financing.
- the lender protection by allowing them to have the loan insured prior to completion of rehabilitation, even before the condition and value of the property may offer adequate security.

 ©All Rights Reserved

- the lender the opportunity to help address climate change by insuring the financing of cost-effective energy efficient improvements.

Why Use 203(k) Program

Homebuyers may face a complicated and costly process or be excluded from certain loan programs to rehabilitate or make property improvements. The 203(k) Program may be a great option for a homeowner who wants to stay in their current home and wants or needs to make improvements.

Borrowers can obtain funds needed to purchase or refinance and renovate based on the appraised value once the proposed improvement is completed. Other home improvement loans often have high interest rates, short repayment terms, or balloon payments.

However, the 203(k) Program offers a solution that helps borrowers by insuring a single, long-term, fixed, or adjustable-rate loan that covers both the acquisition and rehabilitation of a property.

It saves time by combining both the purchase or refinance, with fund for rehabilitation of a property into a single loan instead of typical construction lending with two separate loans. The program saves money with its 3.5% low-down payment, like all FHA-insured mortgages. Also, the rates may be lower than other forms of financing, such as a home equity line of credit or credit cards.

Types of FHA Programs

Standard 203K for major rehabilitation or repairs, and the streamlined/limited 203k for less expensive repairs and updates.

Limited 203(k) Mortgage

- Permits homebuyers and homeowners to finance up to $35,000 into their mortgage to repair, improve, or upgrade their home.
- Homebuyers and homeowners can quickly and easily tap into cash to pay for property repairs or improvements, such as those identified by a home inspector or an FHA appraiser.
- Homeowners can make minor remodeling and non-structural repairs, improvements, or prepare their home for sale.
- Homebuyers can make their new home move-in ready by remodeling the kitchen, painting the interior, or purchasing new carpet.
- FHA-approved 203(k) Consultant is optional for Limited 203(k)
- No minimum amount of repairs required.

 ©All Rights Reserved

This type of rehabilitation loan is the most commonly one used because of the ease of use, and limited repairs needed on the property. When your homebuyer wants to purchase a home and the property inspection or appraiser requires repairs, the homebuyer may include the cost of those repairs in their purchase of the home. The home is appraised with the after-improvement value to help increase the loan amount to cover the costs. The improvements can be as extensive as remodeling a kitchen or as little as replacing an air conditioner. The improvements and repairs must stay under the $35,000 FHA improvement limit.

Streamline 203k program may be used for less extensive repairs that are non-structural in nature like minor remodeling, home improvements, energy efficient improvements, new appliances, or replacing dated carpeting.[121]

Standard 203(k) Mortgage

- The Standard 203(k) program is for major rehabilitation and repair of single-family property.
- The cost of the rehabilitation must be at least $5,000 but the total value of the property must still fall within the FHA mortgage limit for the area.
- The Standard 203(k) program is an important tool for major renovations, structural additions, community, and neighborhood revitalization, as well as to expand homeownership opportunities.[122]
- FHA-approved 203(k) Consultant is required

This rehabilitation program is for major remodeling or rehabilitation of a property. It can take a condemned property and provide the funds to bring it back to a livable space for a family. It can also add a bedroom onto a home that a couple has outgrown. With current unaffordable home prices, it may make more sense if the borrower expands their house footprint to be what they want. There is no limit on the amount of improvements or rehabilitation, provided the loan amount stays within the allowable loan limits for the area and the property appraises to support the rehab.

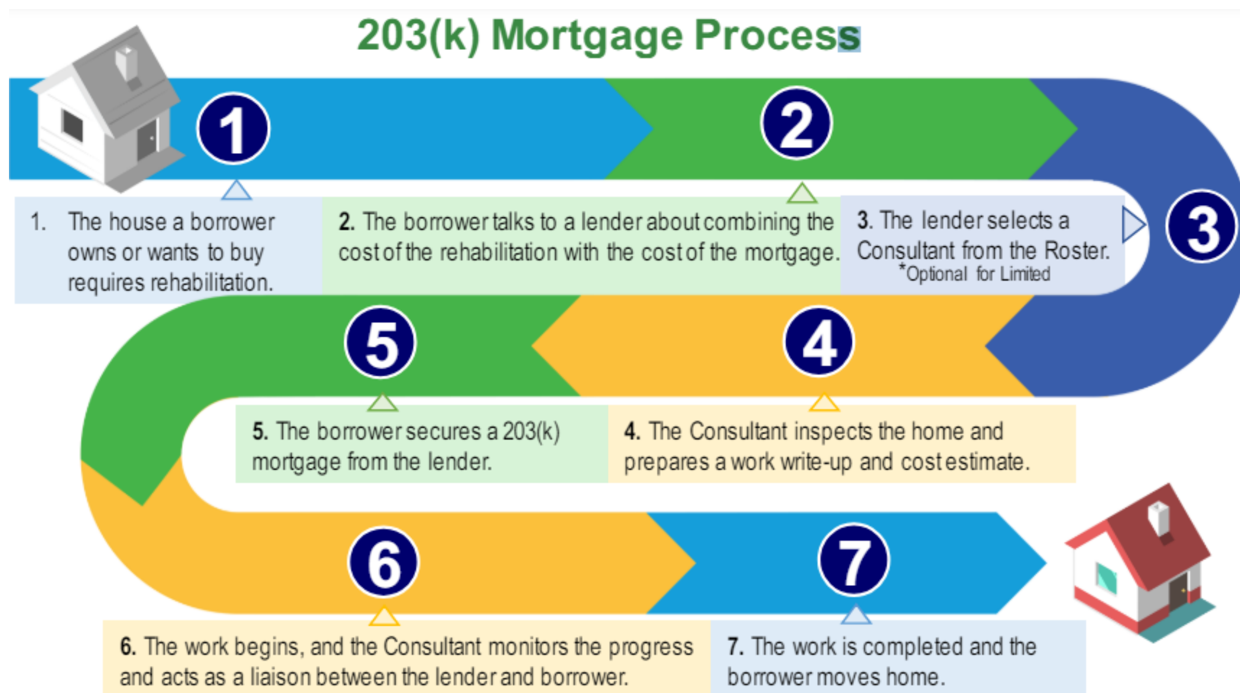
The 203(k) Program requires all building permits be obtained prior to commencement of work and posted onsite for the work being performed.

[121] https://www.hud.gov/sites/dfiles/SFH/documents/MO_FS_203(k)_Consumer.pdf
[122] https://www.hud.gov/program_offices/housing/sfh/203k

©All Rights Reserved

It is important to understand that with rehabilitation programs, the loan closes and the rehabilitation funds go into an escrow account to be disbursed in phases as the home is completed. The lender, MLO and realtor all get paid at closing, so there is no waiting for the home to be completed to get paid. A definite benefit to a realtor. An MLO can also work in revitalization areas to help improve the neighborhood. Churches and other local non-profits are good to partner with for these type of targeted rehab loans promotions.

Stages in the Process



Origination Stage

1. The borrower owns or finds a property that requires rehabilitation.
2. Borrower talks to an FHA-approved lender and selects FHA 203(k) program.
3. Lender selects a 203(k) HUD-approved consultant from the roster. This step is optional for the Limited 203(k) Mortgage.
4. Consultant visits the home with borrower and prepares a work write-up and cost estimate.
5. Work write-up and bids are provided to the lender. This document goes to the appraiser for consideration of the after-value of the property.
6. Lender processes, underwrites, closes, and funds the transaction.
7. The lender submits the loan for endorsement and FHA insures the loan.
8. Improvements can begin.

 ©All Rights Reserved

Repair/Improvements Stage

1. The contractor obtains the necessary permits prior to the start of the project.
2. Contractor completes the first phase of the project.
3. Borrower contacts the 203(k) consultant to request an inspection for draw release.
4. Consultant and borrower inspect the work and consultant certifies work is satisfactory.
5. Consultant and borrower sign the draw release and submit to lender for payment.
6. Lender issues a two-party check made payable to borrower and contractor.
7. This process continues until all work is completed.

Project Completion Stage

1. The borrower provides a release letter indicating all work is completed.
2. Consultant verifies completion.
3. Consultant obtains certificate of occupancy or building permit close-out approval if applicable.
4. Remaining escrow funds are released. If all funds are not used for improvements, the balance is applied to the outstanding principal balance.
5. Lender is responsible for closing out the entire project on the Escrow Close-Out Screen in FHA Connection.
6. 203k provides a maximum of one year to complete the project.

Role of an FHA-Approved 203(k) Consultant

The Consultant plays a guiding role throughout the rehabilitation process, acting as the liaison between the homeowner, contractor(s), and lender. The Consultant inspects the property and prepares a feasibility study, architectural exhibits, work write-ups, cost estimates, draw request inspections, and change orders; and ensures that all work is performed in compliance with FHA requirements. Any Consultant who performs work on a 203(k) project must be listed on the FHA-approved 203(k) Consultant Roster.

203(k) Consultant's Responsibilities Before Loan Closing

Property Inspection and Permits

The Consultant's first task is to personally perform an on-site property inspection, using FHA's 35-Point Checklist, listed in Handbook 4000.1, Section II.A.9.e.

The Consultant must:

©All Rights Reserved

- Address any deficiencies that exist
- Certify the condition of all major systems, health and safety issues, and pests
- Determine any repairs or improvements required to meet HUD's Minimum Property Requirements (MPR) or Minimum Property Standards (MPS) and local requirements
- Ensure all required building permits are obtained before the commencement of work are posted on-site for the work performed

Optional Feasibility Study

If the homebuyer is unsure of the repairs the home will need and their costs, the 203(k) Consultant can complete an optional feasibility study (for a fee) to identify the FHA-required repairs. When the borrower or lender requests to determine if the 203(k) project is financially feasible, the Consultant must prepare a feasibility study. This provides some protection the improvements will be supported in the property's valuation. A borrower may pay additional costs out of pocket if they choose to do so.

Work Write-Up and Cost Estimate

The Consultant must prepare and review the necessary architectural exhibits. If not qualified to prepare them, the Consultant must obtain the architectural exhibits from a qualified subcontractor.

For example - septic certifications, termite reports, foundation certifications, and engineering reports.

Based on this information, the Consultant must prepare a work write-up that addresses any of the work items on the 35-Point Checklist and those on the homeowner's project proposal. On the work write-up, each work item must have a reasonable cost estimate for the area in which the property is located and separately identifies the labor costs and itemized cost of materials. The work write-up and cost estimate must include the work being performed per the project proposal. Health and safety issues must be addressed before any other work items.[123]

203(k) Consultant's Responsibilities After the Mortgage Closes

[123] https://www.hud.gov/sites/dfiles/SFH/documents/MO_203k_CnsltRole_FS.pdf

 ©All Rights Reserved

At mortgage closing, the lender escrows (holds back) the funds designated for rehabilitation. After the escrow is established, the Consultant:

- Reviews the lender request for a draw of funds and must inspect the work for completion and quality of workmanship to ensure the work has been satisfactorily completed in compliance with all codes and ordinances.
- Keeps the lender informed of the progress of the rehabilitation, including any issues that may affect project eligibility, the health, and safety of the homeowner, or work stoppage.
- Reviews any proposed changes and prepares a change order for the lender to approve if changes to the work write-up are requested.

Benefits of Combining the 203K with FHA Energy and Disaster Programs

There are other loan programs offered by FHA that can benefit a borrower when the home they are purchasing needs improvements or repairs. The following FHA home loan programs do not have to be included with the 203k programs.

- **Energy Efficient Mortgages (EEM),** which offers financing of energy efficient improvements with an FHA-insured mortgage. Benefits include cost-effective energy efficient improvements that may lower utility bills and help homeowners save money. Improvements may qualify for Federal, state, and local tax credits.
    - The financed portion of an Energy Package must be cost-effective. Improvements are cost-effective when the cost of making them is equal to or less than the money saved on energy from those improvements. FHA has a cost-effective test for existing homes and newly constructed homes. The program also requires a Home Energy Assessment.
    - The maximum amount of the energy package that can be added to the borrower's regular FHA loan amount is the lesser of:
        - A cost-effective improvements to be made (energy package) based on the home energy assessment; or
        - the lesser of 5 percent of:
            - the Adjusted Value
            - 115 percent of the median area price of a Single-Family dwelling; or
            - 150 percent of the national conforming mortgage limit.

 ©All Rights Reserved

        - An FHA-approved lender can access FHA's EEM Calculator to determine the dollar maximum amount a borrower can finance for energy improvements.[124]
- **Solar and Wind Technologies program**, which offers financing of a new solar energy system with an FHA-insured mortgage at the time of purchase or refinance. Benefits include a reduction in the amount of electricity the consumer buys from their utility provider and the payment on the energy system is spread out over the mortgage term. Improvements may qualify for federal, state, and local tax credits.
    - The full cost of a new solar photovoltaic (PV) array can be added to a regular FHA-insured mortgage at the time of the home purchase or refinance. Installation of the PV system takes place after closing.
    - The solar system must be owned by the borrower and not leased.
    - The amount financed for the new system must not exceed 20% of the property's appraised value.
    - Energy system must be new and not existing.[125]
- **203(h) Mortgage Insurance for Disaster Victims**, which offers financing for the purchase or reconstruction of a single-family property to victims of a Presidentially Declared Major Disaster Area (PDMDA), if obtained within one year of declaration. One of the benefits is that the borrower is not required to make a Minimum Required Investment (MRI), that equates to 100 percent financing.
    - Insured mortgages may be used to finance the purchase or reconstruction of a one-unit family home that will be the principal residence of the homeowner.
    - Home was destroyed or damaged to such an extent that reconstruction or replacement is necessary.
    - No down payment required, eligible for 100% financing. Closing costs and prepaid expenses must be paid by the borrower or paid through premium pricing or by the 6% seller concession limits.[126]

---

[124] https://www.hud.gov/program_offices/housing/sfh/eem/energy-r#:~:text=The%20energy%20package%20is%20the,passive%20solar%20and%20wind%20technologies.
[125] https://www.hud.gov/sites/documents/SOLAR-WIND.PDF
[126] https://www.hud.gov/program_offices/housing/sfh/ins/203h-dft

 ©All Rights Reserved

PACE Loan

Property Assessed Clean Energy Program (PACE) is an innovative mechanism for financing Energy Efficient and renewable energy improvements on private property. A PACE loan gives homeowners a way to borrow money for home improvements by increasing their property tax payment.[127]

The U.S. government does not pay for or insure PACE loans. PACE lending programs are approved by some states and are run by local government, or a private company hired by the local government.

The homeowner pays PACE loans by an additional assessment that is collected with their property taxes. While the consumer may not have to put cash down to pay for these upgrades, they will be required to pay the fees later with their property tax bill. Like a traditional property tax lien, they may lose their home if they don't make the payments. As with any form of financing, consumers should consider the costs and benefits of PACE loans before signing the contract.

Homeowners must make payments for PACE loans through their property taxes which makes their property tax bill go up. For some homeowners, the increase can be large. This could put the homeowner at risk of losing your home through a tax sale. Some other risks include:

- Unaffordable payments
- Limited means to dispute the work or costs once the consumer signs up
- Trouble selling or refinancing the home
- Loss of home equity[128]

Unaffordable Payments

The homeowner pays the PACE loan back plus interest and fees with their property taxes each year until it is paid off. They may have to repay the PACE loan for five, 10, or 20 years. This can lead to high assessments added to their property tax bill. Homeowners should pay attention to how long the PACE loan will last as it may be longer or shorter than other types of loans, which can affect the size of the payments.

[127] https://www.consumerfinance.gov/ask-cfpb/what-is-a-pace-loan-en-1979/
[128] https://www.consumerfinance.gov/ask-cfpb/i-am-considering-a-pace-loan-for-home-improvements-what-should-i-keep-in-mind-before-signing-up-en-2128/

 ©All Rights Reserved

If the homeowner has a mortgage, the mortgage company will treat PACE loans like property taxes, because PACE payment is billed as part of the property tax payment. If the homeowner's home goes to tax sale, any portion of the outstanding PACE loan that is delinquent will be paid before the mortgage company will be paid anything. If the homeowner has an existing mortgage escrow account that collects the tax and insurance payments, most mortgage servicers will add the PACE payments into the mortgage escrow, to make sure that they are paid timely. This would cause the homeowners mortgage payments to rise. Most lenders will not refinance a mortgage or give homeowners a new mortgage if they have an outstanding PACE loan. MLOs should ask all refinance borrowers if they have acquired a PACE loan to ensure their payoff and underwriter guidelines will be met.

If the homeowner does not have an escrow account to collect property tax payments, homeowners will need to save up to make PACE payments along with their property taxes.

If the homeowner does not have a mortgage loan that collects their property tax payments, the homeowner may have to work with the local taxing authority if they fall behind. They may not be able to help beyond offering the homeowner a short-term payment plan, which may not be affordable.

Salespeople may tell the homeowner, but are not required to prove, that the proposed improvements "pay for themselves" in lower utility payments or other rebates. For some projects funded through PACE, these statements may not be true.

Limited Means to Dispute the Work or Costs

Because the homeowner pays PACE loans back with the property taxes, homeowners have limited options when they are not satisfied with the work, wish to dispute the charges, or cannot afford the payments.

Trouble Selling or Refinancing the Home

If the homeowner wants to sell their home before the PACE loan is paid off, they might face challenges completing the sale. When they sell a house, the buyer is responsible for continuing the PACE payments. Any buyer will face the same risks of losing the home if the payments are not made. That may make the home more expensive than buying another home without a PACE loan. Most lenders will not make a mortgage to the buyer when there is a PACE loan on the house.

 ©All Rights Reserved

In addition, most lenders will not refinance a mortgage if there is a PACE loan on the house. This may limit the number of buyers who will be willing to purchase a home if the homeowner cannot afford to pay the PACE loan off.

Loss of Home Equity

If the homeowner's home goes to tax sale, the tax authority will collect any unpaid taxes and any delinquent PACE payments, along with any penalties. This can take a large chunk of any equity in the home. Which means there will be less for the homeowner to use on other expenses.

For example - If the homeowner is planning to use that equity to pay the costs of moving out of the home, or for retirement.[129]

Conventional Rehab Loan

With a conventional rehab loan, the homeowner can finance both the purchase of a new home and the cost of renovations with a single mortgage product. This means the homeowner will not have to take out a second mortgage or pay for costly home improvement projects out of pocket. The funds are provided through private lenders and banks and can be used to pay for cosmetic and structural upgrades.

Here is what to expect with a conventional rehab loan:

Step 1: Apply for a loan product. If borrower is pre-approved, the lender will notify the borrower of the loan terms, including the required down payment.

Step 2: Retrieve contractor plans for the renovation project and submit them to the lender for approval.

Step 3: If the plans are approved, the lender sends an appraiser to assign an after-repair value (that considers the contractor's plans).

Step 4: Close on the home and commence renovations. They should be completed within six months, but some lenders permit the contract to spend up to a year on approved projects.

[129] https://www.consumerfinance.gov/ask-cfpb/i-am-considering-a-pace-loan-for-home-improvements-what-should-i-keep-in-mind-before-signing-up-en-2128/

 ©All Rights Reserved

Types of Conventional Rehab Loans

Homebuyers can choose from two types of conventional rehab loans.

Fannie Mae Home Style Renovation Loan

The Fannie Mae Home Style Renovation Loan can be used to cover upgrade costs on a home the borrower owns or plans to buy. It is limited to 95% of the homes' after-renovation value. The loan comes with an adjustable or fixed interest rate that is typically lower than what they will get with a home equity loan or line of credit. The program is a 15- or 30-year loan term.

Instead of taking out two separate loans, the loan rolls the purchase price and renovation costs into a single mortgage product. That means the borrower only pays closing costs once, and they will have a single monthly housing payment. However, if the borrower has an existing mortgage, they will have to pay it off with this loan, which means the homeowner could end up with a higher mortgage interest rate and payment.

Loans are capped at $766,550 in most markets for single-family properties. However, they could borrow as much as $1,149,825 if the property is in a pricier high-priced real estate markets.

Note, upgrades on manufactured homes are limited to $50,000 or 50% of the anticipated property value after renovations are complete.

This loan program can be used to complete most home upgrades and temporary living expenses during construction within six to 12 months of the closing date. However, borrowers are prohibited from building a second property, making temporary improvements, or demolishing the property with the loan proceeds.[130]

Freddie Mac CHOICE Renovation

The Freddie Mac CHOICE Renovation loan covers renovation costs on owner occupied, investment properties, second homes and multi-unit properties. It allows the homeowner to borrow up to 95% of the home's after-renovation value.

[130] https://www.banks.com/articles/loans/home-improvement/conventional-rehab-loan/

©All Rights Reserved

The homeowner may use the loan proceeds for rehab on a property they are purchasing or already own. An existing property would be considered a refinance requiring the borrower to refinance their existing mortgage which could be at a higher interest rate than they currently have.

The upside is this loan product is it is more flexible than the Fannie Mae Home Style Renovation Loan. The homeowner can use the funds to make most upgrades, and you can cover the costs of renovations that will shield the property from sustaining severe damage if a natural disaster strikes. The cost of repairs for damage caused by natural disasters is also covered.

Loan terms of 15 or 30 years are available. The owner-occupied homeowner will need at least 3.5% down, a credit score of 660, and the debt-to-income ratio should not exceed 43 percent. If the homeowner is planning to complete the renovations before closing, they may be eligible for a down payment credit if they finish the improvement job before closing.[131]

Difference Between a Conventional Loan and a Rehab Loan

A conventional loan is a standard mortgage that is not insured or backed by a government agency. These loans are offered by private lenders and usually require a down payment of around 5% to 20% of the home's value. The terms and requirements for conventional loans can vary depending on the lender, but they have stricter qualifying guidelines than government insured loans.

But a rehab loan is a specialized mortgage that allows the homeowner to finance not only the purchase of a home but also its renovation costs using a single loan.

Advantages of Conventional Rehab Loans

Flexibility of Financing

Conventional rehab loans offer a great deal of flexibility in financing home improvement projects. With these loans, the homeowner can finance both the purchase of a new home and the cost of necessary renovations in a single mortgage product.

This means the homeowner will not need to take out a second mortgage or pay out of pocket for costly renovations. Furthermore, conventional rehab loans are not governed by the same strict rules as government-backed loans, offering them more options and potentially less paperwork.

---

[131] https://www.banks.com/articles/loans/home-improvement/conventional-rehab-loan/

 ©All Rights Reserved

Potential for Property Appreciation

Investing in a fixer-upper with a conventional rehab loan could lead to a significant increase in the property's value because of the improvements made. Since the loan covers both the purchase and renovation costs, the homeowner has the opportunity to transform a distressed property into a valuable asset. As property values rise in the neighborhood, the newly renovated home may appreciate value even more, making it a profitable long-term investment.

Lower Home Ownership Costs

By using a conventional rehab loan for a homeowner's fixer-upper, they can potentially save money on overall homeownership costs.

For example – they might be able to:

- Purchase the property at a lower price: Fixer-uppers are often priced lower than their renovated counterparts, giving homebuyers a chance to buy a property at an affordable price.
- Minimize additional loan expenses: With a single loan instead of multiple loans to finance the purchase and renovation, the homebuyer can avoid multiple closing costs, loan fees, and appraisals.
- Reduce ongoing maintenance costs: By renovating the home upfront with loan funds, the homebuyer can address potential maintenance issues and prevent the need for costly repairs down the line.

Disadvantages of Conventional Rehab Loans

As with any mortgage product, there are also downsides to consider.

- Stricter eligibility guidelines: Conventional rehab loans often have stricter qualification requirements compared to other renovation loan programs, such as FHA 203(k) loans. This means the homebuyer needs a good credit score and stable income to be eligible for a conventional rehab loan. Furthermore, the homebuyer might be required to make a larger down payment than other loan options, which could affect their budget.
- Limited loan amounts: These loans have a cap on the amount of money you can borrow, which may not cover all the desired renovations. Therefore, the homebuyer may need to scale back their plans or find alternative financing options for larger projects.
- More challenging renovation process: Managing the renovation process can be more challenging with a conventional rehab loan. The homeowner will need to collaborate closely

 ©All Rights Reserved

with their contractor to create detailed plans and ensure the work is completed on time and within budget. Some lenders may also require them to work with specific contractors, limiting borrower choices.

Understanding the Loan Process

Qualifying for Conventional Rehab Loans

The homebuyer qualifies for a conventional rehab loan if it meets the criteria below:

- Have good or excellent credit
- Have a down payment of at least five percent
- Have an acceptable debt-to-income ratio

Note - Some lenders require up to 20% down. Even if they qualify for a lower down payment, any amount below 20% requires private mortgage insurance. Also, know that poor credit does not necessarily disqualify a borrower for a loan, but they will need an excellent explanation to convince the lender they are a good candidate for funding.

The Expenses Involved in Rehab Loans

Conventional rehab loans come with several expenses that you should be aware of:

- Down payment: Conventional rehab loans typically require a down payment ranging from 5% to 20% of the total loan amount.
- Closing costs: These may include loan origination fees, appraisal fees, and other expenses related to processing the loan.
- Interest rates: The interest rates for these loans vary based on the borrower's credit rating, loan amount, and other factors.
- Rehabilitation expenses: Homebuyers need to account for the costs involved in renovating the property. As mentioned above, a single mortgage product covers both the purchase and renovation costs.

Alternative to Conventional Rehab Loans

Home equity loans and HELOCs (Home Equity Lines of Credit) are an attractive financing option for many homeowners looking to use their home's equity to make purchases, pay off debt, or finance a renovation. Home equity loans provide borrowers with a lump sum of money that is repaid over a predetermined period at a fixed interest rate. A HELOC works similarly but instead provides a line of

©All Rights Reserved

credit that can be used however the borrower chooses. Both options offer substantial advantages for homeowners, including lower interest rates than most other loan types, flexible repayment plans, and tax benefits.[132]

[132] https://www.banks.com/articles/loans/home-improvement/conventional-rehab-loan/

©All Rights Reserved

Module 4 – Review of Georgia Mortgage Laws

LEARNING OBJECTIVES

- Identify definitions and terms
  - Know those exempt from licensing
  - Have knowledge of the following:
  - Registration, financials and bonds, education, disclosures, annual fees, advertisements, renewal of licenses, record maintenance and applying for licenses
- Understand the automated licensing system

INTRODUCTION

- The contents of this lesson are provided through the Georgia Residential Mortgage Act and the Georgia Mortgage Division Rules.
- The full text of these statutes is available within the resources area of this lesson. Students are strongly encouraged to download and print a copy for further review.
- The Official Codes of Georgia Annotated will be referenced throughout this text as O.C.G.A.

DEFINITIONS [O.C.G.A. §7-1-1000]

Considering there is a lot of jargon when it comes to regulations in the lending industry, it is important to review how some of the terminology used is defined. Section 7-1-1000 of the Official Codes of Georgia Annotated defines the following terminology:

(1) **'Affiliate'** or **'person affiliated with'** means, when used with reference to a specified person, a person who directly, indirectly, or through one or more intermediaries controls, is controlled by, or is under common control with the person specified. Any beneficial owner of 10 percent or more of the securities of a person or any executive officer, director, trustee, joint venturer, or general partner of a person is an affiliate of such person unless the shareholder, executive officer, director, trustee, joint venturer, or general partner shall prove that he or she in fact does not control, is not controlled by, or is not under common control with such person.

(2) **'Audited financial statement'** means the product of the examination of financial statements in accordance with generally accepted auditing standards by an independent certified public accountant, which product consists of an opinion on the financial statements indicating their conformity with generally accepted accounting principles.

©All Rights Reserved

(3) **'Commissioner'** means the commissioner of banking and finance.

(4) **'Commitment' or 'commitment agreement'** means a statement by a lender required to be licensed or registered under this article that sets forth the terms and conditions upon which the lender is willing to make a particular mortgage loan to a particular borrower.

(5) **'Control,'** including **'controlling,' 'controlled by,' and 'under common control with,'** means the direct or indirect possession of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting or nonvoting securities, by contract, or otherwise.

(6) **'Department'** means the Department of Banking and Finance.

(7) **'Depository institution'** has the same meaning as in Section 3 of the Federal Deposit Insurance Act, 12 U.S.C. Section 1813(c), and includes any credit union.

(8) **'Dwelling'** means a residential structure that contains one to four units, whether or not that structure is attached to real property pursuant to Regulation Z Section 226.2(a)(19). The term includes an individual condominium unit, cooperative unit, mobile home, and trailer if it is used as a residence.

(9) **'Executive officer'** means the chief executive officer, the president, the principal financial officer, the principal operating officer, each vice president with responsibility involving policy-making functions for a significant aspect of a person's business, the secretary, the treasurer, or any other person performing similar managerial or supervisory functions with respect to any organization whether incorporated or unincorporated.

(10) **'Extortionate means'** means the use or the threat of violence or other criminal means to cause harm to the person, reputation of the person, or property of the person.

(11) **'Federal banking agencies'** means the Comptroller of the Currency, the Director of the Office of Thrift Supervision, the National Credit Union Administration, and the Federal Deposit Insurance Corporation. Such term shall also include the Board of Governors of the Federal Reserve System.

(12) **'Georgia Residential Mortgage Act'** means this article, which also includes certain provisions in order to implement the federal Secure and Fair Enforcement for Mortgage Licensing Act of 2008.

(13) '**Individual'** means a natural person.

(14) **'License'** means a license issued by the department under this article to act as a mortgage loan originator, mortgage lender, or mortgage broker.

©All Rights Reserved

(15) **'Loan processor or underwriter'** means an individual who performs clerical or support duties as an employee at the direction of and subject to the supervision and instruction of a person licensed or exempt from licensing. For purposes of this paragraph, 'clerical or support duties' may include, subsequent to the receipt of an application, the receipt, collection, distribution, and analysis of information common for the processing or underwriting of a residential mortgage loan; and communicating with a consumer to obtain the information necessary for the processing or underwriting of a loan, to the extent that such communication does not include offering or negotiating loan rates or terms or counseling consumers about residential mortgage loan rates or terms. An individual engaging solely in loan processor or underwriter activities shall not represent to the public, through advertising or other means of communicating or providing information, including the use of business cards, stationery, brochures, signs, rate lists, or other promotional items, that such individual can or will perform any of the activities of a mortgage loan originator.

(16) **'Lock-in agreement'** means a written agreement whereby a lender or a broker required to be licensed or registered under this article guarantees for a specified number of days or until a specified date the availability of a specified rate of interest for a mortgage loan, a specified formula by which the rate of interest will be determined, or a specific number of discount points if the mortgage loan is approved and closed within the stated period of time.

(17) **'Makes a mortgage loan'** means to advance funds, offer to advance funds, or make a commitment to advance funds to an applicant for a mortgage loan.

(18) **'Misrepresent**' means to make a false statement of a substantive fact. Misrepresent may also mean to intentionally engage in any conduct which leads to a false belief which is material to the transaction.

(19) **'Mortgage broker'** means any person who directly or indirectly solicits, processes, places, or negotiates mortgage loans for others, or offers to solicit, process, place, or negotiate mortgage loans for others or who closes mortgage loans which may be in the mortgage broker's own name with funds provided by others and which loans are assigned within 24 hours of the funding of the loans to the mortgage lenders providing the funding of such loans.

(20) **'Mortgage lender**' means any person who directly or indirectly makes, originates, underwrites, or purchases mortgage loans or who services mortgage loans.

(21) **'Mortgage loan'** means a loan or agreement to extend credit made to a natural person,

©All Rights Reserved

which loan is secured by a deed to secure debt, security deed, mortgage, security instrument, deed of trust, or other document representing a security interest or lien upon any interest in one-to- four family residential property located in Georgia, regardless of where made, including the renewal or refinancing of any such loan.

(22) **'Mortgage loan originator'** means an individual who for compensation or gain or in the expectation of compensation or gain takes a residential mortgage loan application or offers or negotiates terms of a residential mortgage loan. Generally, this does not include an individual engaged solely as a loan processor or underwriter except as otherwise provided in paragraph

(5) of subsection (a) of Code Section 7-1-1002; a person or entity that only performs real estate brokerage activities and is licensed or registered in accordance with Georgia law unless the person or entity is compensated by a mortgage lender, mortgage broker, or other mortgage loan originator or by any agent of such mortgage lender, mortgage broker, or other mortgage loan originator; and does not include a person or entity solely involved in extensions of credit relating to time-share plans, as that term is defined in 11 U.S.C. Section 101(53D).

(23) **'Nationwide Multistate Licensing System and Registry'** means a mortgage licensing system developed and maintained by the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators for the licensing and registration of licensed mortgage loan originators, mortgage loan brokers, and mortgage loan lenders.

(24) **'Nontraditional mortgage product'** means any mortgage product other than a 30 year fixed rate mortgage.

(25) **'Person'** means any individual, sole proprietorship, corporation, limited liability company, partnership, trust, or any other group of individuals, however organized.

(26) **'Real estate brokerage activity'** means any activity that involves offering or providing real estate brokerage services to the public, including acting as a real estate agent or real estate broker for a buyer, seller, lessor, or lessee of real property; bringing together parties interested in the sale, purchase, lease, rental, or exchange of real property; negotiating, on behalf of any party, any portion of a contract relating to the sale, purchase, lease, rental, or exchange of real property, other than in connection with providing financing with respect to any such transaction; engaging in any activity for which a person engaged in the activity is required to be registered or licensed as a real estate agent or real estate broker under any

 ©All Rights Reserved

applicable law; and offering to engage in any activity or act in any capacity described herein.

(27) 'Registered mortgage loan originator' means any individual who meets the definition of mortgage loan originator, is registered with and maintains a unique identifier through the Nationwide Multistate Licensing System and Registry, and is an employee of:

a. A depository institution;

b. A subsidiary that is:

i. Owned and controlled by a depository institution; and

ii. Regulated by a federal banking agency; or

c. An institution regulated by the Farm Credit Administration.

(28) 'Registrant' means any person required to register pursuant to Code Sections 7-1-1001 and 7-1-1003.2.

(29) 'Residential property' means improved real property used or occupied, or intended to be used or occupied, as the primary residence of a natural person. Such term does not include rental property or second homes. A natural person can have only one primary residence.

(30) 'Residential mortgage loan' means any loan primarily for personal, family, or household use that is secured by a mortgage, deed of trust, or other equivalent consensual security interest on a dwelling, as defined in Section 103(v) of the Truth in Lending Act, or residential real estate upon which is constructed or intended to be constructed a dwelling.

(31) 'Residential real estate' means any real property located in Georgia upon which is constructed or intended to be constructed a dwelling.

(32) 'Service a mortgage loan' means the collection or remittance for another or the right to collect or remit for another of payments of principal, interest, trust items such as insurance and taxes, and any other payments pursuant to a mortgage loan.

(33) 'Ultimate equitable owner' means a natural person who, directly or indirectly, owns or controls an ownership interest in a corporation or any other form of business organization, regardless of whether such natural person owns or controls such ownership interest through one or more natural persons or one or more proxies, powers of attorney, nominees, corporations, associations, limited liability companies, partnerships, trusts, joint-stock companies, other entities or devices, or any combination thereof.

(34) 'Unique identifier' means a number or other identifier assigned by protocols established by the Nationwide Multistate Licensing System and Registry.

 ©All Rights Reserved

Note: The Georgia State Legislature recently amended these definitions to include “Covered Employee” means any employee of a Mortgage Lender or Mortgage Broker who is involved in residential mortgage-related activities for property located in Georgia and includes, but is not limited to, an originator, mortgage loan processor or underwriter, or other employee who has access to information about the origination, processing or underwriting of residential mortgage loans.

The goal of this was to bring the more restrictive interpretation of Georgia state regulations in line with the national regulations established in the SAFE ACT.

DEFINITIONS [O.C.G.A. §7-6A-2]

In addition, Section 7-6A-2 defines the following terminology:

(1) **'Acceleration'** means a demand for immediate repayment of the entire balance of a home loan.

(2) **'Affiliate'** means any company that controls, is controlled by, or is under common control with another company, as set forth in 12 U.S.C. Section 1841, et seq.

(3) **'Annual percentage rate'** means the annual percentage rate for the loan calculated at closing according to the provisions of 15 U.S.C. Section 1606, the regulations promulgated thereunder by the Board of Governors of the Federal Reserve System, and the Official Staff Commentary on Regulation Z published by the Board of Governors of the Federal Reserve System.

(4) **'Bona fide discount points'** means loan discount points knowingly paid by the borrower for the express purpose of reducing, and which in fact do result in a bona fide reduction of, the interest rate applicable to the home loan; provided, however, that the undiscounted interest rate for the home loan does not exceed by more than one percentage point the required net yield for a 90 day standard mandatory delivery commitment for a home loan with a reasonably comparable term from either the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation, whichever is greater.

(5) **'Borrower'** means any natural person obligated to repay the loan including a co-borrower or cosigner.

(6) '**Creditor'** means a person who both regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments and is a person to whom the debt arising from the home loan transaction is initially payable. Creditor

©All Rights Reserved

shall also mean any person brokering a home loan, which shall include any person who directly or indirectly for compensation solicits, processes, places, or negotiates home loans for others or offers to solicit, process, place, or negotiate home loans for others or who closes home loans which may be in the person's own name with funds provided by others and which loans are thereafter assigned to the person providing the funding of such loans, provided that creditor shall not include a person who is an attorney providing legal services in association with the closing of a home loan. A creditor shall not include: (A) a servicer; (B) an assignee;

(C) a purchaser; or (D) any state or local housing finance agency or any other state or local governmental or quasi-governmental entity.

(7) **'High-cost home loan'** means a home loan in which the terms of the loan meet or exceed one or more of the thresholds as defined in paragraph (17) of this Code section.

(8) **'Home loan'** means a loan, including an open-end credit plan where the principal amount does not exceed the conforming loan size limit for a single-family dwelling as established by the Federal National Mortgage Association and the loan is secured by a mortgage, security deed, or deed to secure debt on real estate located in this state upon which there is located or there is to be located a structure or structures, including a manufactured home, designed principally for occupancy of from one to four families and which is or will be occupied by a borrower as the borrower's principal dwelling, except that home loan shall not include:

A. A reverse mortgage transaction;
B. A loan that provides temporary financing for the acquisition of land by the borrower and initial construction of a borrower's dwelling thereon or the initial construction of a borrower's dwelling on land owned by the borrower;
C. A bridge loan made to a borrower pending the sale of the borrower's principal dwelling or a temporary loan made to a borrower and secured by the borrower's principal dwelling pending the borrower's obtaining permanent financing for such principal dwelling;
D. A loan secured by personal property including, but not limited to, a motor vehicle, motor home, boat, or watercraft and also secured by the borrower's principal dwelling to provide the borrower with potential income tax advantages when such personal property is the primary collateral for such loan;
E. A new loan secured by a borrower's principal dwelling as a result of a lien taken in

 ©All Rights Reserved

connection with a debt previously contracted or incurred when the loan documents for such new loan do not include a mortgage, security deed, or deed to secure debt expressly securing such new loan; or

F. A loan primarily for business, agricultural, or commercial purposes.

(9) 'Make' or 'makes' means to originate a loan or to engage in brokering of a home loan including the soliciting, processing, placing, or negotiating of a home loan made or offered by a person brokering a home loan.

(10) 'Manufactured home' means a structure, transportable in one or more sections, which in the traveling mode is eight body feet or more in width or 40 body feet or more in length or, when erected on site is 320 or more square feet and which is built on a permanent chassis and designed to be used as a dwelling with a permanent foundation when erected on land secured in conjunction with the real property on which the manufactured home is located and connected to the required utilities and includes the plumbing, heating, air-conditioning, and electrical systems contained therein; except that such term shall include any structure which meets all the requirements of this paragraph except the size requirements and with respect to which the manufacturer voluntarily files a certification required by the secretary of the United States Department of Housing and Urban Development and complies with the standards established under the National Manufactured Housing Construction and Safety Standards Act of 1974, 42 U.S.C. Section 5401, et seq. Such term does not include rental property or second homes or manufactured homes when not secured in conjunction with the real property on which the manufactured home is located.

(11) 'Open-end credit plan' or 'open-end loan' means a loan in which (A) a creditor reasonably contemplates repeated transactions; (B) the creditor may impose a finance charge from time to time on an outstanding balance; and (C) the amount of credit that may be extended to the borrower during the term of the loan, up to any limit set by the creditor, is generally made available to the extent that any outstanding balance is repaid.

(12) 'Points and fees' means:

A. All items included in the definition of finance charge in 12 C.F.R. 1026.4(a) and 12 C.F.R. 1026.4(b) except interest or the time price differential. All items excluded under 12 C.F.R. 1026.4(c) are excluded from points and fees, provided that for items under 12 C.F.R. 1026.4(c)(7) the creditor does not receive direct or indirect compensation in connection with the charge and the charge is not paid to an affiliate of the creditor;

©All Rights Reserved

B. All compensation paid directly or indirectly to a mortgage broker from any source, including a broker that originates a loan in its own name in a table funded transaction, including but not limited to yield spread premiums, yield differentials, and service release fees, provided that the portion of any yield spread premium that is both disclosed to the borrower in writing and used to pay bona fide and reasonable fees to a person other than the creditor or an affiliate of the creditor for the following purposes is exempt from inclusion in points and fees: fees for tax payment services; fees for flood certification; fees for pest infestation and flood determination; appraisal fees; fees for inspection performed prior to closing; credit reports; surveys; attorneys' fees, if the borrower has the right to select the attorney from an approved list or otherwise; notary fees; escrow charges, so long as not otherwise included under subparagraph (A) of this paragraph; title insurance premiums; and fire and hazard insurance and flood insurance premiums, provided that the conditions set forth in 12 C.F.R. 1026.4(d)(2) are met;
C. Premiums or other charges for credit life, credit accident, credit health, credit personal property, or credit loss-of-income insurance, debt suspension coverage or debt cancellation coverage, whether or not such coverage is insurance under applicable law, that provides for cancellation of all or part of a borrower's liability in the event of loss of life, health, personal property, or income or in the case of accident written in connection with a home loan and premiums or other charges for life, accident, health, or loss-of- income insurance without regard to the identity of the ultimate beneficiary of such insurance. In determining points and fees for the purposes of this paragraph, premiums or other charges shall only include those payable at or before loan closing and are included whether they are paid in cash or financed and whether the amount represents the entire premium for the coverage or an initial payment.
D. The maximum prepayment fees and penalties that may be charged or collected under the terms of the loan documents. Mortgage interest that may accrue in advance of payment in full of a loan made under a local, state, or federal government sponsored mortgage insurance or guaranty program, including a Federal Housing Administration program, shall not be considered to be a prepayment fee or penalty;
E. All prepayment fees or penalties that are charged to the borrower if the loan refinances a previous loan made or currently held by the same creditor or an affiliate of the creditor;
F. For open-end loans, points and fees are calculated in the same manner as for loans other than open-end loans, based on the minimum points and fees that a borrower would be required to

 ©All Rights Reserved

pay in order to draw on the open-end loan an amount equal to the total credit line; and

G. Points and fees shall not include:
    i. Taxes, filing fees, recording, and other charges and fees paid or to be paid to public officials for determining the existence of or for perfecting, releasing, or satisfying a security interest;
    ii. Bona fide and reasonable fees paid to a person other than the creditor or an affiliate of the creditor for the following: fees for tax payment services; fees for flood certification; fees for pest infestation and flood determination; appraisal fees; fees for inspections performed prior to closing; credit reports; surveys; attorneys' fees, if the borrower has the right to select the attorney from an approved list or otherwise; notary fees; escrow charges, so long as not otherwise included under subparagraph (A) of this paragraph; title insurance premiums; and fire and hazard insurance and flood insurance premiums, provided that the conditions in 12 C.F.R. 1026.4(d)(2) are met;
    iii. Bona fide fees paid to a federal or state government agency that insures payment of some portion of a home loan, including, but not limited to, the Federal Housing Administration, the Department of Veterans Affairs, the United States Department of Agriculture for rural development loans, or the Georgia Housing and Finance Authority; and
    iv. Notwithstanding any provision to the contrary in this chapter, compensation in the form of premiums, commissions, or similar charges paid to a creditor or any affiliate of a creditor for the sale of: (I) title insurance; or (II) insurance against loss of or damage to property or against liability arising out of the ownership or use of property, provided that the conditions in 12 C.F.R. 1026.4(d)(2) are met.

(13) 'Process,' 'processes,' or 'processing' means to act as a processor.

(14) 'Processor' means any person that prepares paperwork necessary for or associated with the closing of a home loan, including but not limited to promissory notes, disclosures, deeds, and closing statements, provided that processor shall not include persons on the grounds that they are engaged in data processing or statement generation services for home loans.

(15) 'Servicer' means the same as set forth in 12 C.F.R. 1024.2.

(16) 'Servicing' means the same as set forth in 12 C.F.R. 1024.2.

(17) '**Threshold'** means:

 ©All Rights Reserved

A. Without regard to whether the loan transaction is or may be a 'residential mortgage transaction' as that term is defined in 12 Section C.F.R. 1026.2(a)(24), the annual percentage rate of the loan is such that it equals or exceeds that set out in Section 152 of the Home Ownership and Equity Protection Act of 1994, 15 U.S.C. Section 1602(bb), and the regulations adopted pursuant thereto by the Federal Reserve Board, including 12 C.F.R. Section 1026.32; or

B. The total points and fees payable in connection with the loan, excluding not more than two bona fide discount points, exceed: (i) 5 percent of the total loan amount if the total loan amount is $20,000.00 or more or (ii) the lesser of 8 percent of the total loan amount or $1,000.00 if the total loan amount is less than $20,000.00.

(18) 'Total loan amount' means the amount calculated as set forth in 12 C.F.R. 1026.32(a) and under the Official Staff Commentary of the Board of Governors of the Federal Reserve System. For open-end loans, the total loan amount shall be calculated using the total credit line available under the terms of the home loan as the amount financed.

Now that we have reviewed relevant terminology, we should move on to determine what the law specifically states regarding registration and licensing.

Exemptions; Registration Requirements [O.C.G.A. §7-1-1001]

a. According to the law, the following persons shall not be required to obtain a mortgage loan originator, broker, or mortgage lender license. However, they may be subject to registration requirements, if registration of such persons is required by this article:

1. Any lender authorized to engage in business as a bank, credit card bank, savings institution, building and loan association, or credit union under the laws of the United States, any state or territory of the United States, or the District of Columbia, the deposits of which are federally insured;
2. Any wholly owned subsidiary of any lender described in paragraph (1) of this Code section. Any subsidiary that violates any applicable law of this article may be subject to a cease and desist order as provided for in Code Section 7-1-1018;

2.1 Any wholly owned subsidiary of any bank holding company; provided, however, that such subsidiary shall be subject to registration requirements in order to facilitate the department's handling of consumer inquiries. Such requirements are contained in Code

©All Rights Reserved

Section 7-1-1003.3;

3. Registered mortgage loan originators, when acting for an entity described in paragraphs (1) or (2) of this Code section. To qualify for this exemption, an individual shall be registered with and maintain a unique identifier through registration with the Nationwide Multistate Licensing System and Registry;
4. Any individual who offers or negotiates terms of a residential mortgage loan with or on behalf of an immediate family member of such individual. For purposes of this exemption, the term 'immediate family member' means a spouse, child, sibling, parent, grandparent, or grandchild. Immediate family members shall include stepparents, stepchildren, stepsiblings, and adoptive relationships;
5. A licensed attorney who negotiates the terms of a residential mortgage loan on behalf of a client as an ancillary matter to the attorney's representation of the client, unless the attorney is compensated by a lender, a mortgage broker, or other mortgage loan originator or by any agent of such lender, mortgage broker, or other mortgage loan originator;
6. A Georgia licensed real estate broker or real estate salesperson not actively engaged in the business of negotiating mortgage loans or a Georgia licensed real estate salesperson providing information to a lender or its agent related to an existing or potential short sale transaction in which a separate fee is not received by such real estate broker or real estate salesperson; provided, however, that such real estate broker or real estate salesperson who directly or indirectly negotiates, places, or finds a mortgage for others shall not be exempt from the provisions of this article;
7. Any person performing any act relating to mortgage loans under order of any court;
8. Any natural person or the estate of or trust created by a natural person making a mortgage loan with his or her own funds for his or her own investment, including those natural persons or the estates of or trusts created by such natural persons who make a purchase money mortgage for financing sales of their own property;
9. Any agency, division, or instrumentality of the federal government of the United States of America; the government of the State of Georgia; the government of any other state of the United States; or any county or municipal of the State of Georgia. This includes, but is not limited to the Georgia Housing and Finance Authority, the Georgia Development Authority, the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC), the Government National Mortgage Association (GNMA), the United States

©All Rights Reserved

Department of Housing and Urban Development (HUD), the Federal Housing Administration (FHA), the Department of Veterans Affairs (VA), the Farmers Home Administration (FmHA), and the Farm Credit Administration and its chartered agricultural credit associations;

10. Any individual who offers or negotiates terms of a residential mortgage loan secured by a dwelling that serves as the individual's residence;
11. Any person who makes a mortgage loan to an employee of such person as an employment benefit;
12. Any licensee under Chapter 3 of this title, the "Georgia Installment Loan Act," provided that any mortgage loan made by such licensee is for $3,000.00 or less;
13. Nonprofit corporations making mortgage loans to promote home ownership or improvements for the disadvantaged.
14. A natural person employed by a licensed or registered mortgage broker, a licensed or registered mortgage lender, or any person exempted from the mortgage broker or mortgage lender licensing requirements of this article when acting within the scope of employment and under the supervision of the mortgage broker or mortgage lender or exempted person as an employee and not as an independent contractor, except those natural persons exempt from licensure as a mortgage broker or mortgage lender under paragraph (17) of this Code section. To be exempt from licensure as a mortgage broker or mortgage lender, a natural person shall be employed by only one such employer and shall be at all times eligible for employment in compliance with the provisions and prohibitions of Code Section 7-1-1004. Such natural person, who meets the definition of mortgage loan originator provided in paragraph (22) of Code Section 7-1-1000, shall be

    subject to mortgage loan originator licensing requirements. A natural person against whom a cease and desist order has become final shall not qualify for this exemption while under the employment time restrictions of subsection (o) of Code Section 7-1- 1004 if such order was based on a violation of Code Section 7-1-1002 or 7-1-1013 or whose license was revoked within five years of the date such person was hired;
15. Any person who purchases mortgage loans from a mortgage broker or mortgage lender solely as an investment and who is not in the business of brokering, making, purchasing, or servicing mortgage loans;
16. Any natural person who makes five or fewer mortgage loans in any one calendar year. A person other than a natural person who makes five or fewer mortgage loans in any one

©All Rights Reserved

calendar year shall not be exempt from the licensing requirements of this article; or

17. (A)

A natural person who is under an exclusive written independent contractor agreement with any person that is a licensed mortgage broker, so long as such licensed mortgage broker also meets the following requirements, subject to the review and approval of the department:

(i) The licensee continuously provides a surety bond as required by Code Section 7-1-1003.2 in the amount of $150,000.00 plus $50,000.00 per exempt natural person, not to exceed a maximum of $2 million to cover its activities as well as the activities of all of its natural persons exempted by this paragraph;

(ii) The licensee has applied for and been granted a mortgage broker license, consistent with the provisions of this article and renewable annually;

(iii) The licensee has paid applicable fees for this license, which license fees shall be the sum of the cost of the individual mortgage broker license fees if each exempt natural person received a mortgage broker license;

(iv) The licensee has full and direct financial responsibility for the mortgage activities of such natural person and full and direct responsibility for the proper education of such natural person, the handling of consumer complaints related to such natural person, and the supervision of the mortgage activities of such natural person. The licensee shall supervise such natural person on an ongoing and regular basis and shall be accountable for the mortgage activities of such natural person;

(v) The licensee or the parent company if the licensee is a wholly owned subsidiary:

(I) Files reports under Section 13(a) or 15(d) of the Securities Exchange Act of 1934;

(II) Has a market capitalization in excess of $4 billion at the time of the initial application for a mortgage broker license based on the number of outstanding shares at the end of the quarter as disclosed in the most recent Form 10-Q filed with the United States Securities and Exchange Commission; and

(III) Has equity securities that are listed on the New York Stock Exchange, the National Association of Securities Dealers Automated Quotations, or other stock market approved by the department in writing;

(vi) At the time of the initial application for a mortgage broker license, the licensee has never had a mortgage lender license or mortgage broker license revoked or suspended in Georgia or any other state;

©All Rights Reserved

(vii) The licensee, the parent company if the licensee is a wholly owned subsidiary, or an affiliate of the licensee if both the affiliate and licensee are wholly owned subsidiaries of the same parent company, is licensed by the office of the Commissioner of Insurance as an insurance company or is registered with the Secretary of State as a broker-dealer;

(viii) The licensee is licensed as a mortgage lender or mortgage broker in ten or more states; and

(ix) At the time of the initial application for a mortgage broker license, the licensee has received at least a satisfactory evaluation in the most recent examination conducted by the majority of the states in which it has a mortgage broker or mortgage lender license and has adequately addressed with the department any unsatisfactory evaluations in the most recent examination conducted by any state in which it has a mortgage broker or mortgage lender license.

(B) To maintain the exemption, a natural person shall:

(i) Solicit, process, place, or negotiate a mortgage loan to be brokered only by the licensee;

(ii) Be at all times in compliance with this article, including the provisions and prohibitions of Code Section 7-1-1013, the provisions and prohibitions applicable to employees under Code Section 7-1-1004, and the department's rules and regulations;

(iii) Be licensed as a mortgage loan originator in Georgia and work exclusively for the licensee, the parent company if the licensee is a wholly owned subsidiary, or an affiliate of the licensee if both the affiliate and licensee are wholly owned subsidiaries of the same parent company; and

(iv) Be licensed as an insurance agent with the office of the Commissioner of Insurance or registered as a broker-dealer agent with the Secretary of State on behalf of the licensee, the parent company of the licensee if the licensee is a wholly owned subsidiary of the parent company, or an affiliate of the licensee if both the affiliate and licensee are wholly owned subsidiaries of the same parent company.

18. (A) An employee of a bona fide nonprofit corporation who acts as a mortgage loan originator only with respect to his or her work duties with the bona fide nonprofit corporation and who acts as a mortgage loan originator only with respect to mortgage loans with terms that are favorable to the borrower shall be exempt from obtaining a mortgage loan originator license. In order for a corporation to be considered a bona fide nonprofit corporation under

©All Rights Reserved

this paragraph, the department shall determine, under criteria and pursuant to processes established by the department, that the nonprofit corporation:

i. Has the status of a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code of 1986;
ii. Promotes affordable housing;
iii. Conducts its activities in a manner that serves public or charitable purposes, rather than commercial purposes;
iv. Receives funding and revenue and charges fees in a manner that does not incentivize it or its employees to act other than in the best interests of its clients;
v. Compensates its employees in a manner that does not incentivize employees to act other than in the best interests of its clients;
vi. Provides or identifies for the borrower mortgage loans with terms favorable to the borrower and comparable to mortgage loans and housing assistance provided under government housing assistance programs. In order for mortgage loans to have terms that are favorable to the borrower, the department shall determine that the terms are consistent with loan origination in a public or charitable context, rather than in a commercial context; and
vii. Satisfies the exemption from licensure set forth in paragraph (13) of this subsection.

(B) The department shall periodically examine the books and activities of an organization it has previously identified as a bona fide nonprofit corporation for purposes of this paragraph in order to determine if it continues to meet the criteria for such status under subparagraph (A) of this paragraph. In conducting such an examination, the department shall have all of the powers set forth in Code Section 7-1-1009. In the event the nonprofit corporation no longer qualifies for such status, then the employee exemption from having a mortgage loan originator license shall no longer be applicable; or

(19) Any person who purchases or holds closed mortgage loans for the sole purpose of securitization into a secondary market, provided that such person holds the individual loans for less than seven days.

©All Rights Reserved

b. Exemptions enumerated in paragraphs (1), (2), (2.1), (7), (8), (9), (11), (12), (13), (14), (15), (16), and (17) of subsection (a) of this Code section shall be exemptions from licensure as a mortgage broker or mortgage lender only. Nothing in paragraphs (1), (2), (2.1), (7), (8), (9), (11), (12), (13), (14), (15), (16), and (17) of subsection (a) of this Code section shall be intended to exempt natural persons from compliance with mortgage loan originator licensing requirements as set forth in this article and the Secure and Fair Enforcement for Mortgage Licensing Act of 2008. Individuals that transact business as a mortgage loan originator, unless specifically exempted by paragraph (3), (4), (5), (6), (10), or (18) of subsection (a) of this Code section, shall obtain a mortgage loan originator license as required by Code Section 7-1-1002 whether they are employed by a mortgage broker, mortgage lender, or person exempted as a mortgage broker or lender as set forth in this subsection.

c. A licensed mortgage lender is authorized to engage in all activities that are authorized for a mortgage broker and, as a result, shall not be required to obtain a mortgage broker license.

d. Any violation of this article or the rules and regulations of the department by a natural person exempted pursuant to paragraph (17) of subsection (a) of this Code section shall be deemed to be a violation by both the licensee and the exempt natural person for purposes of the enforcement provisions of this article.

The above lists the type of people that are not legally required to obtain a license in order to do conduct their actives. Let's now turn to those which the law imposes a license requirement.

Requirements for MLO License [O.C.G.A. §7-1-1001.1]

To comply with the federal requirements contained in the Secure and Fair Enforcement for Mortgage Licensing Act of 2008, also known as the S.A.F.E. Mortgage Licensing Act of 2008, it is now prohibited for any person to engage in the activities of a mortgage loan originator without first obtaining and maintaining a mortgage loan originator license.

The department has the broad administrative authority to administer, interpret, and enforce the SAFE Mortgage Licensing Act of 2008, and promulgate rules and regulations implementing it. The provisions in the SAFE Act apply to the activities of retail sellers of manufactured homes to the extent determined by the United States Department of Housing and Urban Development through written guidelines, rules, regulations, or interpretive letters.

Therefore, since one must be licensed in order to conduct mortgage loan originator duties, it is no surprise that the law goes on to state the following:

©All Rights Reserved

a. It shall be prohibited for any person to transact business in this state directly or indirectly as a mortgage broker, a mortgage lender, or a mortgage loan originator unless such person:
    1. Is licensed or registered as such by the department utilizing the Nationwide Multistate Licensing System and Registry;
    2. Is a person exempted from the licensing or registration requirements pursuant to Code Section 7-1-1001;
    3. In the case of an employee of a mortgage broker or mortgage lender, such person has qualified to be relieved of the necessity for a license under the employee exemption in paragraph (11) of subsection (a) of Code Section 7-1-1001;
    4. In the case of a mortgage loan originator, such person is supervised by a mortgage broker, mortgage lender, or exemptee on a daily basis while performing mortgage functions; is employed by and works exclusively for only one mortgage broker, mortgage lender, or exemptee; and is paid on a W-2 basis by the employing mortgage broker, mortgage lender, or exemptee, except those natural persons exempt from licensure as a mortgage broker or mortgage lender under paragraph (17) of subsection
    (a) of Code Section 7-1-1001. Each licensed mortgage loan originator shall register with and maintain a valid unique identifier issued by the Nationwide Multistate Licensing System and Registry. For the purposes of implementing an orderly and efficient mortgage loan originator process, the department may establish licensing rules or regulations and interim procedures for licensing and acceptance of applications; or
b. A loan processor or underwriter who is an independent contractor shall not engage in the activities of a loan processor or underwriter unless such independent contractor loan processor or underwriter obtains and maintains a mortgage broker or mortgage lender license. Each independent contractor loan processor or underwriter licensed as a mortgage broker or mortgage lender shall have and maintain a valid unique identifier issued by the Nationwide Multistate Licensing System and Registry.
c. It shall be prohibited for any person, as defined in Code Section 7-1-1000, to purchase, sell, or transfer one or more mortgage loans or loan applications from or to a mortgage loan originator, mortgage broker, or mortgage lender who is neither licensed nor exempt from

 ©All Rights Reserved

the licensing or registration provisions of this article. Such a purchase shall not affect the obligation of the borrower under the terms of the mortgage loan. The department shall provide for distribution or availability of information regarding approved or revoked licenses.

d. Every person who directly or indirectly controls a person who violates subsection (a) or (b) of this Code section, every general partner, executive officer, joint venturer, or director of such person, and every person occupying a similar status or performing similar functions as such person violates with and to the same extent as such person, unless the person whose violation arises under this subsection sustains the burden of proof that he or she did not know and, in the exercise of reasonable care, could not have known of the existence of the facts by reason of which the original violation is alleged to exist.

As you can see, the law is very specific regarding who must be licensed and who is exempted from this requirement. It is crucial that a person understand what mortgage loan originator activities are in order to determine whether they must be licensed or registered to continue conducting certain activities or whether they are not required to be licensed or registered in order to continue doing what they are doing. If a person is caught conducting mortgage loan originator activities without a license, that person will subject to punishment by law.

Application for Licenses [O.C.G.A. §7-1-1003]

As mentioned previously, the department has authority to prescribe licenses. As such, they are responsible for reviewing applications. The law states that applications for licensure must include the following:

The legal name and address of the applicant and, if the applicant is a partnership, association, corporation, or other business entity, of every member, officer, and director thereof;

1. All names, including, but not limited to, website domain names (URLs), under which the applicant will conduct business in Georgia;
2. For mortgage brokers and mortgage lenders, the address of the main office or principal place of business where books and records are located and any other locations at which the applicant will engage in any business activity covered by the provisions of this article, together with the mailing address where the department shall send all correspondence, orders, or notices. Any changes in this mailing address shall be delivered in writing to the department before the change is effective;
3. For mortgage brokers and mortgage lenders, the complete name and address of the

©All Rights Reserved

applicant's initial registered agent and registered office for service of process in Georgia. If the applicant is a Georgia corporation, this registered agent shall be the same as the agent recorded with the Secretary of State. Any changes in the registered agent or registered office shall be delivered in writing to the department and the Secretary of State, if applicable, before the change is effective. The registered agent may, but is not required to, be an officer of the applicant, and the registered office shall be a Georgia location where the registered agent may be served;

4. For mortgage brokers and mortgage lenders, the general plan and character of the business;
5. For mortgage brokers and mortgage lenders, a financial statement of the applicant;
6. For mortgage brokers and mortgage lenders, such other data, financial statements, and pertinent information as the department may require with respect to the applicant, its directors, trustees, officers, members, agents, or ultimate equitable owners of 10 percent or more of the applicant; and
7. For mortgage brokers and mortgage loan originators, evidence of satisfaction of experience or education requirements, as required by regulations of the department.

b. All applications filed under this Code section shall be filed together with:
    1. Investigation and supervision fees established by regulation;
    2. The items required by Code Section 7-1-1003.2;
    3. Other information as may be required by the department.

Financial Requirements; Bond Requirements [O.C.G.A. §7-1-1003.2]

The law imposes certain financial requirements on those that want to become licensed. The law states the following:

a. Each licensed or registered mortgage broker shall provide the department with a bond. The bond for a mortgage broker shall be in the principal sum of $150,000.00 or such greater sum as the department may require as set forth by regulation based on an amount that reflects the dollar amount of loans originated, and the bond shall meet the other requirements of subsection (d) of this Code section.
b. Except as otherwise provided in subsection (d) of this Code section, the department shall

©All Rights Reserved

not license or register any mortgage lender unless the applicant or registrant provides the department with a bond. The bond for a mortgage lender shall be in the principal sum of $250,000.00 or such greater sum as the department may require as set forth by regulation based on an amount that reflects the dollar amount of loans originated, and which bond shall meet the other requirements of subsection (d) of this Code section.

c. Each mortgage loan originator shall be covered by a surety bond of his or her sponsoring licensed or registered mortgage broker or lender. In the event that the mortgage loan originator is an employee of a licensed or registered mortgage broker or lender or under an exclusive written independent contractor agreement as described in paragraph (17) of Code Section 7-1- 1001, the surety bond of such licensed or registered mortgage broker or lender may be used in lieu of the mortgage loan originator's surety bond requirement.
d. General bond requirements:
    1. The bond requirements for mortgage loan originators, mortgage brokers, and mortgage lenders are continuous in nature and shall be maintained at all times as a condition of licensure;
    2. The corporate surety bond shall be for a term and in a form satisfactory to the department, shall be issued by a bonding company or insurance company authorized to do business in this state and approved by the department, and shall run to the State of Georgia for the benefit of any person damaged by noncompliance of a licensee with this article, the 'Georgia Residential Mortgage Act,' or with any condition of such bond. Damages under the bond shall include moneys owed to the department for fees, fines, or penalties. Such bond shall be continuously maintained thereafter in full force. Such bond shall be conditioned upon the applicant or the licensee conducting his or her licensed business in conformity with this article and all applicable laws;
    3. When an action is commenced on a licensee's bond, the department may require the filing of a new bond; and
    4. Immediately upon recovery of any action on the bond, the licensee shall file a new bond.
e. Any person including the department who may be damaged by noncompliance of a licensee with any condition of a bond or this article, the 'Georgia Residential Mortgage Act,' may proceed on such bond against the principal or surety thereon, or both, to

 ©All Rights Reserved

recover damages.

Application for Registration [O.C.G.A. §7-1-1003.3]

According to law, any application to register as a mortgage lender or broker must be made annually in writing, under oath, and on a form provided by the department. The application is subject to requirements specified by rules and regulations of the department.

Therefore, if you are already registered, you must apply to be registered yearly.

This process is different for those applying for licensure as mortgage loan originators, mortgage brokers, and mortgage lenders.

We will discuss the application and renewal process for mortgage loan originators, brokers, and lenders later. We will next review the extent of the authority given to the department by law with regards to licensing.

Automated Licensing System for MLOs, Mortgage Brokers and Mortgage Lenders [O.C.G.A. §7-1-1003.5]

The law states that the department is authorized to do all of the following:

1. Participate in a Nationwide Multistate Licensing System and Registry established to facilitate the sharing of information and standardization of the licensing and application processes for mortgage loan originators, mortgage brokers, and mortgage lenders by electronic or other means;
2. Enter into operating agreements, information sharing agreements, interstate cooperative agreements, and other contracts necessary for the department's participation in the Nationwide Multistate Licensing System and Registry;
3. Request that the Nationwide Multistate Licensing System and Registry adopts an appropriate privacy, data security, and security breach notification policy that is in full compliance with existing state and federal law;
4. Disclose or cause to be disclosed without liability via the Nationwide Multistate Licensing System and Registry applicant and licensee information, including, but not limited to, violations of this article and enforcement actions, via the Nationwide Multistate Licensing System and Registry to facilitate regulatory oversight of mortgage loan originators, mortgage brokers, and mortgage lenders across state jurisdictional lines;

 ©All Rights Reserved

5. Establish and adopt, by rule or regulation, requirements for participation by applicants and licensees in the Nationwide Multistate Licensing System and Registry upon the department's determination that each new or amended requirement is consistent with both the public interest and the purposes of this article; and
6. Pay all fees received from licensees and applicants related to applications, licenses, and renewals to the Office of Treasury and Fiscal Services; provided, however, that the department may net such fees to recover the cost of participation in the Nationwide Multistate Licensing System and Registry; and

As you can see, the department has a lot of power when it comes to the licensing of mortgage loan originators, brokers, and lenders. In fact, the law also makes clear how much power the department has by stating that regardless of the department's participation in NMLS&R, it retains full and exclusive determinations whether to grant, renew, suspend, or revoke licenses issued to mortgage loan originators, mortgage brokers, and mortgage lenders. Nothing in this section of Georgia law can reduce this authority.

Investigations; Education and Other Requirements [O.C.G.A. §7-1-1004]

The law also specifically provides the department with the authority to establish any requirements it deems necessary for the application for license or registration:

a. Upon receipt of an application for license or registration, the department shall conduct such investigation as it deems necessary to determine that the mortgage broker and mortgage lender applicant and the individuals who direct the affairs or establish policy for the mortgage broker and mortgage lender applicant, including the officers, directors, or the equivalent, are of good character and ethical reputation; that the mortgage broker and mortgage lender applicant is not disqualified for licensure as a result of adverse administrative civil or criminal findings in any jurisdiction; that the mortgage broker and mortgage lender applicant and such persons meet the requirements of subsection (h) of this Code section; that the mortgage broker and mortgage lender applicant and such persons demonstrate reasonable financial responsibility; that the mortgage broker and mortgage lender applicant has reasonable policies and procedures to receive and process customer grievances and inquiries promptly and fairly; and that the mortgage broker and mortgage lender applicant has and maintains a registered agent for service

©All Rights Reserved

in this state.

b. The department shall not license or register any mortgage broker and mortgage lender applicant unless it is satisfied that the mortgage broker and mortgage lender applicant may be expected to operate its mortgage lending or brokerage activities in compliance with the laws of this state and in a manner which protects the contractual and property rights of the citizens of this state.
c. The department may establish by rule or regulation minimum education or experience requirements for an applicant for a mortgage broker license or renewal of such a license.
d. To this end, the law provides that the department must do whatever is necessary to determine that the applicant has completed all requirements for licensure. Once an application for a mortgage loan originator license is submitted, the department must make sure that the applicant:
    1. Has never had a mortgage loan originator license revoked in any governmental jurisdiction, except that a subsequent formal vacation of such revocation shall not be deemed a revocation;
    2. Has not been convicted of, or pled guilty or nolo contendere to, a felony in a domestic, foreign, or military court; provided, however, that any pardon of a conviction shall not be a conviction for purposes of this subsection;
    3. Has demonstrated financial responsibility, character, and general fitness such as to command the confidence of the community and to warrant a determination that the mortgage loan originator will operate honestly, fairly, and efficiently within the purposes of this article;
    4. Has completed the pre-licensing education requirement described in subsection (e) of this Code section;
    5. Has passed a written test that meets the test requirement described in subsection (f) of this Code section; and
e. (1) An individual shall complete at least 20 hours of pre-licensing education courses reviewed and approved by the Nationwide Multistate Licensing System and Registry based upon reasonable standards. Review and approval of a pre-licensing education course shall include review and approval of the course provider. The 20 hours of pre-licensing education shall include at least:
    A. Three hours of federal law and regulations;

©All Rights Reserved

B. Three hours of ethics, which shall include instruction on fraud, consumer protection, and fair lending issues; and
C. Two hours of training related to lending standards for the nontraditional mortgage product marketplace.

2. Nothing in this subsection shall preclude any pre-licensing education course, as approved by the Nationwide Multistate Licensing System and Registry, that is provided by the employer of the mortgage loan originator applicant or an entity which is affiliated with the applicant by an agency contract, or any subsidiary or affiliate of such employer or entity.
3. Pre-licensing education may be offered either in a classroom, online, or by any other means approved by the Nationwide Multistate Licensing System and Registry.
4. The pre-licensing education requirements approved by the Nationwide Multistate Licensing System and Registry in paragraph (1) of this Code section for any state shall be accepted as credit towards completion of pre-licensing education requirements in Georgia.
5. A person previously licensed under this article subsequent to January 1, 2010, applying to be licensed again shall prove that they have completed all of the continuing education requirements for the year in which the license was last held.
6. The department is authorized to enact rules and regulations related to the expiration of pre-licensing education

f.

1. In order to meet the written test requirement referred to in subsection (d) of this Code section for mortgage loan originators, an individual shall pass, in accordance with the standards established under this subsection, a qualified written test developed by the Nationwide Multistate Licensing System and Registry and administered by a test provider approved by the Nationwide Multistate Licensing System and Registry based upon reasonable standards.
2. A written test shall not be treated as a qualified written test for purposes of this subsection unless the test adequately measures the applicant's knowledge and comprehension in appropriate subject areas, including:
   A. Ethics;
   B. Federal law and regulation pertaining to mortgage origination;

©All Rights Reserved

C. State law and regulation pertaining to mortgage origination; and
D. Federal and state law and regulation, including instruction on fraud, consumer protection, the nontraditional mortgage marketplace, and fair lending issues.

3. Nothing in this subsection shall prohibit a test provider approved by the Nationwide Multistate Licensing System and Registry from providing a test at the location of the employer of the applicant or the location of any subsidiary or affiliate of the employer of the applicant or the location of any entity with which the applicant holds an exclusive arrangement to conduct the business of a mortgage loan originator.
4. (A) An individual shall not be considered to have passed a qualified written test unless the individual achieves a test score of not less than 75 percent correct answers to questions.
   B. An individual may retake a test three consecutive times with each consecutive taking occurring at least 30 days after the preceding test.
   C. After failing three consecutive tests, an individual shall wait at least six months before taking the test again.
   D. A licensed mortgage loan originator who fails to maintain a valid license for a period of five years or longer shall retake the test, not taking into account any time during which such individual is a registered mortgage loan originator.

Uniform State Test (UST)

- The Uniform State Test (UST)
  - This is a section within the National Test
  - Georgia has a UST state test with only one exam for licensing
  - Will include 25 questions
    - National Test with UST will contain 120 questions total
    - Grade is a total of all questions
  - This material will test an applicant's knowledge of state-related content and CSBS/AARMR Model State Law (MSL)
  - Replaces the state-specific test section for those states choosing to implement it
  - A person who passes the National Test with UST content or the Stand-

©All Rights Reserved

alone UST will have satisfied requirements for a license in that state

Points "d," "e," and "f"" list the requirements necessary in order to obtain a mortgage loan originator license. If the department finds that any of these requirements have not been met, then the department reserves the right to deny the application for licensure.

This section of the law also provides the requirements necessary to renew a license after having obtained one.

g. (1) In order to meet the annual continuing education requirements referred to in paragraph (2) of subsection (e) of Code Section 7-1-1005, a licensed mortgage loan originator shall complete at least eight hours of education approved in accordance with paragraph (2) of this subsection which shall include at least:

    A. Three hours of federal law and regulations;
    B. Two hours of ethics, which shall include instruction on fraud, consumer protection, and fair lending issues; and
    C. Two hours of training related to lending standards for the nontraditional mortgage product marketplace.

2. For purposes of paragraph (1) of this subsection, continuing education courses shall be reviewed and approved by the Nationwide Multistate Licensing System and Registry based upon reasonable standards. Review and approval of a continuing education course shall include review and approval of the course provider.
3. Nothing in this subsection shall preclude any education course from approval by the Nationwide Multistate Licensing System and Registry that is provided by the employer of the mortgage loan originator or any entity which is affiliated with the mortgage loan originator by an agency contact, or any subsidiary or affiliate of such employer or entity.
4. Continuing education may be offered either in a classroom, online, or by any other means approved by the Nationwide Multistate Licensing System and Registry.
5. A licensed mortgage loan originator, except for as provided for in paragraph (9) of this subsection and subsection (f) of Code Section 7-1-1005, shall only receive credit for a continuing education course in the year in which the course is taken and shall not take the same approved course in the same or successive years to

©All Rights Reserved

meet the annual requirements for continuing education.

6. A licensed mortgage loan originator who is an approved instructor of an approved continuing education course may receive credit for the licensed mortgage loan originator's own annual continuing education requirement at the rate of two hours of credit for every one hour taught.
7. An individual having successfully completed the education requirements approved by the Nationwide Multistate Licensing System and Registry in paragraph (1) of this subsection for any state shall be accepted as credit towards completion of continuing education requirements in Georgia.
8. A licensed mortgage loan originator who subsequently becomes unlicensed shall complete the continuing education requirements for the last year in which the license was held prior to issuance of a new or renewed license.
9. An individual meeting the requirements of subsection (e) of Code Section 7-1-1005 may make up any deficiency in continuing education as established by rule or regulation of the department.

h. The department shall not issue or may revoke a license or registration if it finds that the mortgage loan originator, mortgage broker, or mortgage lender applicant or licensee, or any person who is a director, officer, partner, covered employee, or ultimate equitable owner of 10 percent or more of the mortgage broker or mortgage lender applicant, registrant, or licensee or any individual who directs the affairs or establishes policy for the mortgage broker or mortgage lender applicant, registrant, or licensee, has been convicted of a felony in any jurisdiction or of a crime which, if committed within this state, would constitute a felony under the laws of this state.

i. Fees for background checks that the department administers shall be sent to the department by applicants and licensees together with the fingerprints. Mortgage broker and mortgage lender applicants, licensees, and registrants shall have the primary responsibility for obtaining background checks of covered employees which are defined as employees who work in this state and also have the authority to enter, delete, or verify any information on any mortgage loan application form or document. The department shall, however, retain the right to obtain conviction data on covered employees.

j. In connection with an application for licensing with respect to any mortgage loan originator applicant, mortgage broker, or lender applicant, at the direction of the department, the

 ©All Rights Reserved

applicant shall at a minimum, furnish to the Nationwide Multistate Licensing System and Registry information concerning the applicant's identity, including:

1. Fingerprints for submission to the Federal Bureau of Investigation, and any governmental agency or entity authorized to receive such information for a state, national, and international criminal history background check; and
2. Personal history and experience in a form prescribed by the Nationwide Multistate Licensing System and Registry, including the submission of authorization for the Nationwide Multistate Licensing System and Registry and the department to obtain;
    A. An independent credit report obtained from a consumer reporting agency described in section 603(p) of the Fair Credit Reporting Act, 15 U.S.C. Section 1681a(f); and
    B. Information related to any administrative, civil, or criminal findings by any governmental jurisdiction.
3. For the purposes set forth in this subsection and in order to reduce the points of contact which the Federal Bureau of Investigation may have to maintain for purposes of such section, the department may use the Nationwide Multistate Licensing System and Registry as a channeling agent for requesting information from and distributing information to the Department of Justice or any governmental agency; and
4. For the purposes of this subsection and in order to reduce the points of contact which the department may have to maintain for purposes of such subsection, the department may use the Nationwide Multistate Licensing System and Registry as a channeling agent for requesting and distributing information to and from any source so directed by the department.

k. Every mortgage broker and mortgage lender licensee, registrant, and applicant shall be authorized and required to obtain background checks on covered employees. Such background checks shall be handled by the Georgia Crime Information Center pursuant to Code Section 35-3-34 and the rules and regulations of the Georgia Crime Information Center. Licensees, registrants, and applicants shall be responsible for any applicable fees charged by the center. A background check shall be initiated for a person in the employ of a licensee, registrant, or applicant within ten days of the date of initial hire and be completed with satisfactory results within the first 90 days of employment. This provision shall not apply to directors, officers, partners, agents, or ultimate equitable owners of 10 percent or more or to persons who direct

 ©All Rights Reserved

the company's affairs or establish policy, whose background shall have been investigated through the department before taking office, beginning employment, or securing ownership. Upon receipt of information from the Georgia Crime Information Center that is incomplete or that indicates an employee has a criminal record in any state other than Georgia, the employer shall submit to the department two complete sets of fingerprints of such person, together with the applicable fees and any other required information. The department shall submit such fingerprints as provided in subsection (i) of this Code section.

l. Upon receipt of fingerprints, fees, and other required information, the Georgia Crime Information Center shall promptly transmit one set of fingerprints to the Federal Bureau of Investigation for a search of bureau records and an appropriate report and shall retain the other set and promptly conduct a search of its own records and records to which it has access. The Georgia Crime Information Center shall notify the department in writing of any derogatory finding, including, but not limited to, any conviction data regarding the fingerprint records check, or if there is no such finding. All conviction data received by the department or by the applicant, registrant, or licensee shall be used by the party requesting such data for the exclusive purpose of carrying out the responsibilities of this article, shall not be a public record, shall be privileged, and shall not be disclosed to any other person or agency except to any person or agency which otherwise has a legal right to inspect the file. The department shall be entitled to review any applicant's, registrant's, or licensee's files to determine whether the required background checks have been run and whether all covered employees are qualified. The department shall be authorized to discuss the status of employee background checks with licensees. All such records shall be maintained by the department and the applicant or licensee or registrant pursuant to laws regarding such records and the rules and regulations of the Federal Bureau of Investigation and the Georgia Crime Information Center, as applicable. As used in this subsection, "conviction data" means a record of a finding, verdict, or plea of guilty or plea of nolo contendere with regard to any crime, regardless of whether an appeal of the conviction has been sought, subject to the conditions set forth in subsection (h) of this Code section. Violation of this Code section may subject a licensee or registrant to the revocation of its license or registration.

m. In connection with an application for licensing or registration under this Code section, the department may use the Nationwide Multistate Licensing System and Registry, when such service is available, as a channeling agent for the submission of fingerprints to the Federal

 ©All Rights Reserved

Bureau of Investigation and any governmental agency or entity authorized to receive such information for a state, national, and international criminal history background check. The department is authorized to set forth rules and regulations in order to implement the provisions of this subsection.

n. The department may deny or revoke a license or registration or otherwise restrict a license or registration if it finds that the mortgage broker or mortgage lender applicant or any person who is a director, officer, partner, or ultimate equitable owner of 10 percent or more or person who directs the company's affairs or who establishes policy of the applicant has been in one or more of these roles as a mortgage lender, broker, or registrant whose license or registration has been denied, revoked, or suspended within five years of the date of the application.

o. The department shall not issue a license or registration to and may revoke a license or registration from a mortgage broker or mortgage lender applicant, licensee, or registrant if such person:

    1. Has been the recipient of a final cease and desist order issued within the preceding five years if such order was based on a violation of subsection (h) of this Code section or Code Section 7-1-1002 or 7-1-1013;
    2. Employs any other person against whom a final cease and desist order has been issued within the preceding five years if such order was based on a violation of subsection (h) of this Code section or Code Section 7-1-1002 or 7-1-1013; or
    3. Has had his or her license revoked within five years of the date such person was hired or employs any other person who has had his or her license revoked within five years of the date such person was hired.

p. Each mortgage broker and mortgage lender applicant, licensee, and registrant shall, before hiring an employee, examine the department's public records to determine that such employee is not subject to the type of cease and desist order described of this Code section.

q. Within 90 days after receipt of a completed application and payment of licensing fees prescribed by this article, the department shall either grant or deny the request for license or registration.

r. A person shall not be indemnified for any act covered by this article or for any fine or penalty incurred pursuant to this article as a result of any violation of the law or regulations contained in this article, due to the legal form, corporate structure, or choice of organization of such person, including, but not limited to, a limited liability company.

©All Rights Reserved

So there you have it, folks! What we just went over spells out the specific requirements to obtain a license and retain one as a mortgage loan originator, mortgage broker, or mortgage lender. For the purposes of doing so, the department is granted full authority in the decision making of granting, renewing, or revoking licensure.

Of course, the Nationwide Multistate Licensing System and Registry is in place for a reason and the law does place responsibilities on brokers and lenders to provide certain things to the NMLS&R. For example, the law requires that Each mortgage broker and mortgage lender shall submit to the Nationwide Multistate Licensing System and Registry reports of condition, which shall be in such form and shall contain such information as the department and the Nationwide Multistate Licensing System and Registry may require. **[O.C.G.A. §7-1-1004.1]**

The law also places responsibility on the department to establish a process whereby licensees may challenge information that is entered in the Nationwide Multistate Licensing System and Registry by the department. **[O.C.G.A. §7-1-1004.2]**

For the purposes of ensuring that accountability is met and in order to make the NMLS&R function as it is intended, it is important that the unique identifier of any person originating a residential mortgage loan shall be clearly shown on all residential mortgage loan application forms, solicitations, or advertisements, including business cards, websites, and any other documents as established by rule, regulation, or order of the department. **[O.C.G.A. §7-1-1004.3]**

We already discussed some of the requirements purported by law for the renewal of a license or registration. However, the law does pose additional requirements regarding the timeframe for renewal. We will review this next.

Renewal of Licenses and Registrations [O.C.G.A. 7-1-1005]

a. All licenses and registrations issued pursuant to this article shall expire on December 31 of each year, and application for renewal shall be made annually on or before December 1 of each year.
b. Any licensee or registrant making proper application on or before December 1 for the renewal of a license or registration for the following calendar year shall be permitted to continue to operate pending final approval or disapproval of the application if the application for the license or registration is not acted upon prior to January 1. For purposes of this subsection, a 'proper application' shall include a requirement that all documentation requesting a renewal has been completed, the requisite continuing education has been

 ©All Rights Reserved

successfully obtained, and payment has been made of all outstanding fines and applicable fees required by this article.

c. No investigation fee shall be payable in connection with the renewal application, but an annual license or registration fee established by regulation of the department to defray the cost of supervision shall be paid with each renewal application, which fee shall not be refunded.
d. Any person holding a license or registration pursuant to this article who fails to file a proper application for a license or registration renewal for the following license year, including the proper fee accompanying the application, on or before December 1 and who files an application after December 1 may be required to pay, in addition to the license or registration fees, a fine in an amount to be established by regulations promulgated by the department.
e. The minimum standards for license renewal for mortgage loan originators shall include:
    1. The mortgage loan originator continues to meet the minimum standards for license issuance;
    2. The mortgage loan originator has satisfied the annual continuing education requirements; and
    3. The mortgage loan originator has paid all required fees for renewal of the license;
    4. The mortgage loan originator is in compliance with any and all written orders issued by the department.
f. A mortgage loan originator license shall become inactive in the event that the mortgage loan originator is no longer sponsored by a mortgage lender or mortgage broker that is licensed. A mortgage loan originator shall not act as a mortgage loan originator in this state while the license is inactive. A mortgage loan originator license shall remain in inactive status until the license expires pursuant to subsection (a) of this Code section, the licensee surrenders the license, the license is revoked or suspended, or the licensee obtains sponsorship.
g. The department may adopt procedures for the reinstatement of expired licenses consistent with the standards established by the Nationwide Multistate Licensing System and Registry.

We now know the necessary requirements for license renewal. Let's move on to discussing some of the responsibilities licensees have once they have obtained their license.

 ©All Rights Reserved

Contents of License; Posting of License; etc. [O.C.G.A. §7-1-1006]

a. Each license issued under this article shall state the name of the licensee.
b. A licensee shall post a copy of such license in a conspicuous place in each place of business of the licensee.
c. A license shall not be transferred or assigned.
d. No licensee shall transact business under any name or names other than those designated in the records of the department.
e. For mortgage brokers and mortgage lenders, each licensee shall notify the department in writing of any change in the address of the principal place of business or of any additional location of business in Georgia, any change in registered agent or registered office, any change of executive officer or contact person for consumer complaints, or of any material change in the licensee's financial statement. Notice of changes shall be received by the department no later than 30 business days after the change is effective.
f. without prior approval of the department. Applications for such additional office shall be made in writing on a form prescribed by the department and shall be accompanied by payment of a $350.00 nonrefundable application fee. The application shall be approved unless the department finds that the applicant has not conducted business under this article efficiently, fairly, in the public interest, and in accordance with law. The application shall be deemed approved if notice to the contrary has not been mailed by the department to the applicant within 45 days of the date the application is received by the department.
g. All branch managers in Georgia shall be approved by the department. A mortgage broker or mortgage lender may place a new branch manager subject to the department's approval but shall file for approval within 15 days of the placement and shall remove the person immediately should the department deny approval.

Licensee To Give Notice of Certain Actions [O.C.G.A. §7-1-1007]

Additionally, the law requires licensees to provide notice to the department of certain actions

For example, a licensee must give written notice to the department of any action which may be brought against it by any creditor or borrower where such action is brought under this article, involves a claim against the bond filed with the department for the purposes of compliance with Code Section 7-1-1003.2 or 7-1-1004, or involves a claim for damages in excess of $25,000.00 for a mortgage broker or mortgage loan originator and $250,000.00 for a lender and of any judgment

©All Rights Reserved

which may be entered against it by any creditor or any borrower or prospective borrower, with details sufficient to identify the action or judgment, within 30 days after the commencement of any such action or the entry of any such judgment.

The same is the case for a corporate surety. A corporate surety shall, within ten days after it pays any claim to any claimant, give written notice to the department of such payment with details sufficient to identify the claimant and the claim or judgment so paid. Whenever the principal sum of such bond is reduced by one or more recoveries or payments thereon, the mortgage loan originator, mortgage broker, or mortgage lender shall furnish a new or additional bond so that the total or aggregate principal sum of such bond or bonds shall equal the sum required under Code Section 7-1-1003.2 or 7-1-1004 or shall furnish an endorsement duly executed by the corporate surety reinstating the bond to the required principal sum thereof.

Also, if a bond filed must be canceled by either the mortgage loan originator, mortgage broker, or mortgage lender or the corporate surety, the department must be notified before doing so. The department must be notified electronically through the Nationwide Multistate Licensing System and Registry, the cancellation to be effective not less than 30 days after receipt by the department of such notice and only with respect to any breach of condition occurring after the effective date of such cancellation.

Additionally, the law states that:

a. A licensee or registrant shall, within ten days after knowledge of the event, report in writing to the department:
    1. Any knowledge or discovery of an act prohibited by Code Section 7-1-1013;
    2. The discharge of any employee for dishonest or fraudulent acts; and
    3. Any administrative, civil, or criminal action initiated against the licensee, registrant, or any of its control persons by any government entity.

    Any person reporting such an event shall be protected from civil liability as provided in Code Section 7-1-1009.

<u>Record Maintenance</u> [O.C.G.A. §7-1-1009]

As you know, there are certain record keeping requirements for licensees. This section of the law states the following regarding record maintenance:

 ©All Rights Reserved

a. Mortgage brokers and mortgage lenders required to be licensed or registered under this article shall maintain at their offices or such other location as the department shall permit such books, accounts, and records as the department may reasonably require in order to determine whether such mortgage brokers and mortgage lenders are complying with the provisions of this article and rules and regulations adopted in furtherance thereof. Such books, accounts, and records shall be maintained separately and distinctly from any other personal or unrelated business matters in which the mortgage brokers and mortgage lenders are involved.
b. The department may, by its designated officers and employees, as often as it deems necessary, but at least once every 24 months, investigate and examine the affairs, business, premises, and records of any mortgage broker or mortgage lender required to be licensed or registered under this article insofar as such affairs, business, premises, and records pertain to any business for which a license or registration is required by this article. Notwithstanding the provisions of this subsection, the department has the discretion to examine a mortgage broker or mortgage lender less frequently, provided that its record of complaints, comments, or other information demonstrates that mortgage broker's or mortgage lender's ability to meet the standards of Code Sections 7-1-1003, 7-1-1003.2, and 7-1-1004. In the case of registrants, the department shall not be required to conduct such examinations if it determines that the registrant has been adequately examined by another bank regulatory agency. In order to avoid unnecessary duplication of examinations, the department may accept examination reports performed and produced by other state or federal agencies, unless the department determines that the examinations are not available or do not provide information necessary to fulfill the responsibilities of the department under this article.
c. In addition to any authority allowed under this article, the department shall be authorized to conduct investigations and examinations of mortgage loan originators as follows:
    1. For purposes of initial licensing, license renewal, license suspension, license conditioning, license revocation or termination, or general or specific inquiry or investigation to determine compliance with this article, the department shall have the authority to access, receive, and use any books, accounts, records, files, documents, information, or evidence, including, but not limited to:
        A. Criminal, civil, and administrative history information, including nonconviction data;

 ©All Rights Reserved

B. Personal history and experience information, including independent credit reports obtained from a consumer reporting agency described in section 603(p) of the Fair Credit Reporting Act, 15 U.S.C. Section 1681a(f); and
C. Any other documents, information, or evidence the department deems relevant to the inquiry or investigation regardless of the location, possession, control, or custody of such documents, information, or evidence;

2. For the purposes of investigating violations or complaints, or for the purposes of examination, the department may review, investigate, or examine any mortgage loan originator licensee, individual, or person subject to this article as often as necessary in order to carry out the purposes of this article. The department may direct, subpoena, or order the attendance of and examine under oath all persons whose testimony may be required about the loans or the business or subject matter of any such examination or investigation and may direct, subpoena, or order such person to produce books, accounts, records, files, and any other documents the department deems relevant to the inquiry;
3. Each mortgage loan originator licensee, individual, or person subject to this article shall make available to the department upon request the books and records relating to the activities of a mortgage loan originator;
4. Each mortgage loan originator subject to this article shall make or compile reports or prepare other information as directed by the commissioner in order to carry out the purposes of this subsection, including, but not limited to:
   A. Accounting compilations;
   B. Information lists and data concerning loan transactions in a format prescribed by the department; or
   C. Use, hire, contract, or employ public or privately available analytical systems, methods, or software to examine or investigate a mortgage loan originator;
5. In making any examination or investigation authorized by this article, the department may control access to any documents and records of the licensee or person under investigation. In order to carry out the purposes of this Code section, the department may:
   A. Enter into agreements or relationships with other government officials or

©All Rights Reserved

regulatory associations in order to improve efficiencies and reduce regulatory burden by sharing resources, standardized or uniform methods or procedures, and documents, records, information, or evidence obtained under this Code section;

B. Accept and rely on examination or investigation reports made by other government officials, within or without this state; and

C. Accept audit reports made by an independent certified public accountant for the licensee, individual, or person subject to this article in the course of that part of the examination covering the same general subject matter as the audit and may incorporate the audit report in the report of examination, report of investigation, or other writing of the department;

6. The authority to investigate provided for in this subsection shall remain in effect whether such licensee, individual, or person subject to this article acts or claims to act under any licensing or registration law of this state or claims to act without such authority; and
7. No mortgage loan originator licensee, individual, or person subject to investigation or examination under this article shall knowingly withhold, abstract, remove, mutilate, destroy, or secrete any books, records, computer records, or other information.

d. The department, at its discretion, may:

1. Make such public or private investigations within or outside of this state as it deems necessary to determine whether any person has violated or is about to violate this article or any rule, regulation, or order under this article, to aid in the enforcement of this article, or to assist in the prescribing of rules and regulations pursuant to this article;
2. Require or permit any person to file a statement in writing, under oath or otherwise as the department determines, as to all the facts and circumstances concerning the matter to be investigated;
3. Disclose information concerning any violation of this article or any rule, regulation, or order under this article, provided the information is derived from a final order of the department;
4. Disclose the imposition of an administrative fine or penalty under this article; and
5. Conduct an on-site examination without prior notice, with the licensee or registrant to pay the reasonably incurred costs for such examination, including out-of-state travel expenses,

©All Rights Reserved

and the department shall be authorized to net such out-of-state expenses against the payments from the licensee or registrant.

e.

1. For the purpose of conducting any investigation as provided in this Code section, the department shall have the power to administer oaths, to call any party to testify under oath in the course of such investigations, to require the attendance of witnesses, to require the production of books, records, and papers, and to take the depositions of witnesses; and for such purposes, the department is authorized to issue a subpoena for any witness or for the production of documentary evidence. Such subpoenas may be served by certified mail or statutory overnight delivery, return receipt requested, to the addressee's business mailing address, by examiners appointed by the department, or shall be directed for service to the sheriff of the county where such witness resides or is found or where the person in custody of any books, records, or paper resides or is found. The required fees and mileage of the sheriff, witness, or person shall be paid from the funds in the state treasury for the use of the department in the same manner that other expenses of the department are paid.
2. The department may issue and apply to enforce subpoenas in this state at the request of a government agency regulating mortgage lenders or brokers of another state if the activities constituting the alleged violation for which the information is sought would be a violation of this article if the activities had occurred in this state.

f. In case of refusal to obey a subpoena issued under this article to any person, a superior court of appropriate jurisdiction, upon application by the department, may issue to the person an order requiring him or her to appear before the court to show cause why he or she should not be held in contempt for refusal to obey the subpoena. Failure to obey a subpoena may be punished as contempt by the court.

g. Examinations and investigations conducted under this article and information obtained by the department in the course of its duties under this article are confidential, except as provided in this subsection, pursuant to the provisions of Code Section 7-1-70. In addition to the exceptions set forth in subsection (b) of Code Section 7-1-70 and in paragraphs (3) and (4) of subsection (d) of this Code section, the department is authorized to share information obtained under this article with other state and federal regulatory agencies or law enforcement authorities. In the case of such sharing, the safeguards to confidentiality already in place within such agencies or

 ©All Rights Reserved

authorities shall be deemed adequate. The commissioner or an examiner specifically designated may disclose such limited information as is necessary to conduct a civil or administrative investigation or proceeding. Information contained in the records of the department which is not confidential and may be made available to the public either on the department's website, upon receipt by the department of a written request, or in the Nationwide Multistate Licensing System and Registry shall include:

1. For mortgage brokers and mortgage lenders, the name, business address, and telephone, facsimile, and unique identifier of a licensee or registrant;
2. For mortgage brokers and mortgage lenders, the names and titles of the principal officers;
3. For mortgage brokers and mortgage lenders, the name of the owner or owners thereof;
4. For mortgage brokers and mortgage lenders, the business address of a licensee's or registrant's agent for service; and
5. The terms of or a copy of any bond filed by a licensee or registrant.

h. In the absence of malice, fraud, or bad faith, a person shall not be subject to civil liability arising from the filing of a complaint with the department or furnishing other information required by this Code section or required by the department under the authority granted in this article. No civil cause of action of any nature shall arise against such person:

1. For any information relating to suspected prohibited acts furnished to or received from law enforcement officials, their agents, or employees or to or from other regulatory or licensing authorities;
2. For any such information furnished to or received from other persons subject to the provisions of this title; or
3. For any such information furnished in complaints filed with the department.

i. The commissioner or any employee or agent shall not be subject to civil liability, and no civil cause of action of any nature exists against such persons arising out of the performance of activities or duties under this article or by publication of any report of activities under this Code section.

Annual Financial Statements [O.C.G.A. §7-1-1010]

In addition to having to keep certain records in case of investigation, certain records must be created and kept for delivery to the department.

 ©All Rights Reserved

For example:

a. If a mortgage broker is a United States Department of Housing and Urban Development loan correspondent, such broker shall also submit to the department the audit that is required for the United States Department of Housing and Urban Development. The department may require the mortgage broker to have made an audit of the books and affairs of the licensed or registered business and submit to the department an audited financial statement if the department finds that such an audit is necessary to determine whether the mortgage broker is complying with the provisions of this article and the rules and regulations adopted in furtherance of this article.
b. Each mortgage lender licensed or registered under this article shall at least once each year have made an audit of the books and affairs of the licensed or registered business and submit to the department at renewal an audited financial statement, except that a mortgage lender licensed or registered under this article which is a subsidiary shall comply with this provision by annually providing a consolidated audited financial statement of its parent company and a financial statement, which may be unaudited, of the licensee or registrant which is prepared in

   accordance with generally accepted accounting principles. A lender who utilizes a bond in lieu of an audit need not supply such audit, unless specially required by the department. An audit shall be less than 15 months old to be acceptable. The department may by regulation establish additional minimum standards for audits and reports under this Code section.

Annual Fees [O.C.G.A. §7-1-1011]

As with everything, obtaining, retaining, and using a license does come with certain financial obligations.

The law enables the department to prescribe annual fees to be paid by licensees and registrants, which fees shall be set at levels necessary to defray costs and expenses incurred by the state in providing the examinations and supervision required by this article and its federally mandated participation in the Nationwide Multistate Licensing System and Registry.

The law also imposes certain fees to the borrower instead of the mortgage loan originator, broker, or lender:

The law imposes a fee on the borrower during the closing of every mortgage loan subject to regulation under this article which, as defined in Code Section 7-1-1000, includes all mortgage

 ©All Rights Reserved

loans, whether or not closed by a mortgage broker or mortgage lender licensee or registrant, a fee of

$10.00. The fee shall be paid by the borrower to the collecting agent at the time of closing of the mortgage loan transaction. The collecting agent shall remit the fee to the department at the time and in the manner specified by regulation of the department. Revenue collected by the department pursuant to this subsection shall be deposited in the general fund of the state.

- As used in this subsection, the term "collecting agent" means the person listed as the secured party on a security deed or other loan document that establishes a lien on the residential real property taken as collateral at the time of the closing of the mortgage loan transaction.
- The fee mentioned above included in the closing of a loan is meant to be a debt from the borrower to the collecting agent until such assessment is paid and shall be recoverable at law in the same manner as authorized for the recovery of other debts. Any collecting agent who neglects, fails, or refuses to collect the fee imposed by this subsection shall be liable for the payment of the fee.

Disclosure Requirements [O.C.G.A. §7-1-1014]

Aside from other rules, regulations, and policies that the department may promulgate to effectuate the purpose of this article, the department can also promulgate regulations governing the disclosures that must be provided for applicants for mortgage loans, including the following requirements:

1. Any person required to be licensed or registered under this article shall provide to each applicant for a mortgage loan prior to accepting an application fee or any third-party fee such as a property appraisal fee, credit report fee, or any other similar fee a disclosure of the fees payable and the conditions under which such fees may be refundable;
2. Any mortgage lender required to be licensed or registered under this article shall make available to each applicant for a mortgage loan at or before the time a commitment to make a mortgage loan is given a written disclosure of the fees to be paid in connection with the commitment and the loan, or the manner in which such fees shall be determined and the conditions under which such fees may be refundable; and
3. Any mortgage lender required to be licensed or registered under this article shall disclose to each borrower of a mortgage loan that failure to meet every condition of the mortgage loan may result in the loss of the borrower's property through foreclosure. The

borrower shall be required to sign the disclosure at or before the time of the closing of the mortgage loan.

The department may prescribe standards regarding the accuracy of required disclosures and may provide for applicable administrative or civil penalties or fines for failure to provide the disclosures or to meet the prescribed standards.

Regulations Relative to Advertising [O.C.G.A. §7-1-1016]

There are also specific provisions regarding advertising that the department has the authority to create and enforce. The department shall prescribe regulations governing the advertising of mortgage loans, including, without limitation, the following requirements:

1. (A) Advertisements for loans regulated under this article shall not be false, misleading, or deceptive. No person whose activities are regulated under this article shall advertise in any manner so as to indicate or imply that its interest rates or charges for loans are in any way recommended,' 'approved,' 'set,' or 'established' by the state or this article.

   B. An advertisement shall not include an individual's loan number, loan amount, or other publicly available information unless it is clearly and conspicuously stated in boldface type at the beginning of the advertisement that the person disseminating it is not authorized by, in sponsorship with, or otherwise affiliated with the individual's lender, which shall be identified by name. Such an advertisement shall also state that the loan information contained therein was not provided by the recipient's lender;

2. All advertisements, including websites, disseminated by a licensee or a registrant in this state by any means shall contain the name, license number, Nationwide Multistate Licensing System and Registry unique identifier, and an office address of such licensee or registrant, which shall conform to a name and address on record with the department; and

Advertising Requirements

[Georgia Department of Banking and Finance-Mortgage Division Rules 80-11-1-.02]

There is a lot of advertising involved in the lending industry, therefore making it crucial for proper consumer protection laws to be available and easily enforced. These provisions exist on the federal level. With regards to provisions in the state of Georgia, the following provisions are in place in an effort to protect the consumer:

a. Advertisements for mortgage loans shall not be false, misleading, or deceptive.

 ©All Rights Reserved

b. Advertisements for mortgage loans shall not indicate in any manner that the interest rates or charges for loans are in any way recommended, approved, set or established by the state or by any law of the state.

c. All solicitations or advertisements, including business cards and websites, for mortgage loans disseminated in this state by persons required to be licensed or registered under O.C.G.A. Title 7, Chapter 1, Article 13 shall contain the name, license number, valid unique Nationwide Multistate Licensing System and Registry (NMLSR) identifier, and an office address of the licensee or registrant advertising the mortgage loan, which name, address, and license number shall conform with the name, license number, valid unique NMLSR identifier and office address on record with the Department of Banking and Finance.

d. All advertisements disseminated in this state by persons required to be licensed under

   O.C.G.A. Title 7, Chapter 1, Article 13 in any media, whether print or electronic, shall contain the words "Georgia Residential Mortgage Licensee" or, if an entity is licensed in more than one state, the licensee's advertisement may list Georgia as a state in which the licensee is licensed.

e. All advertisements for mortgage loans shall comply with all applicable federal and state laws.

f. For purposes of this Rule, "advertisement" means material used or intended to be used to induce the public to apply for a mortgage loan. Such term shall include any printed or published material, audio or visual material, website, or descriptive literature concerning a mortgage loan subject to regulation under O.C.G.A. Title 7, Chapter 1, Article 13 whether disseminated by direct mail, newspaper, magazine, radio or television broadcast, electronic, billboard or similar display. The term advertisement shall not include promotional materials containing fifteen words or fewer relating to the mortgage business of the entity which material does not contain references to a specific rate or product, such as balloons, hats, pencils or pens, and calendars.

g. Every mortgage broker or mortgage lender required to be licensed or registered shall maintain a record of samples of its advertisements (including commercial scripts of all radio and television broadcasts) for examination by the Department of Banking and Finance.

h. An advertisement shall not include an individual’s loan number, loan amount, or other publicly available information unless it is clearly and conspicuously stated in bold-faced

©All Rights Reserved

type at the beginning of the advertisement that the person disseminating it is not authorized by, acting on behalf of, or otherwise affiliated with the individual's lender, which shall be identified by name. Such an advertisement shall also state that the loan information contained therein was not provided by the recipient's lender.

 ©All Rights Reserved