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Monday, August 13, 2007

Office of Chief Counsel
Department of Banking
Attention: Public Comment on Regulation 3-43 17
N. Second Street, Suite 1300
Harrisburg, PA 17101-2290

RE: Pennsylvania Financial Services Association
Comments on Proposed Amendments
Chapter 46 of Title 10

Dear Counselor:

The Pennsylvania Financial Services Association ("PFSA") believes that the proposed amendments to Chapter 46 of the regulations as proposed in 37 Pa.B. 3416 on July 21, 2007 have merit and in general they are supported by its members. However, there are some comments that the members believe must be taken into consideration before final adoption could be supported[1].

The suggested changes to the language of the proposal are set forth below, followed by an explanation of the reason(s) for the suggested change.

CLARIFICATION OF DISCLOSURE PROCEDURES

"§46.2(b) *Disclosures to applicant.* (i) On a form or forms prescribed by the Department and signed and dated by the applicant and the licensee, a licensee who has direct contact with the applicant shall disclose the following items to the applicant no later than three business days after the application is received or prepared by the licensee if all of the items to be disclosed have been determined. In the event that one or more of such items has not been determined by the lender which will be providing the loan, or the licensee with direct contact with the applicant has not been advised of such determination at the time that this disclosure is required, then the

[1] PFSA would point out to the department that the "Statement on Subprime Mortgage Lending" was issued by federal regulatory agencies on July 10, 2007, Federal Register/ Vol. 72, No. 131, as the department is no doubt aware. That statement affects federally regulated lenders and the department is urged to attempt to make this regulation consistent therewith to prevent consumer confusion from differing standards. We have attempted to make our comments consistent in that regard.

disclosure form prescribed by the Department shall state that these items must be determined by the licensee providing the loan and must be disclosed to the applicant when so determined, but not later than 5 business days prior to the closing of the loan transaction if by mail, or 3 business days prior to closing if by personal delivery, overnight delivery service, email, facsimile, or other electronic means. Disclosures of such items shall be provided no later than 3 business days after all of such information is determined by the licensee providing the loan either by the licensee who has direct contact with the applicant or the licensee providing the loan as the case may be. The items to be disclosed hereunder are:

(1) If the lender providing the loan will escrow the applicable taxes and insurance.

(2) If the licensee is a lender with the ability to directly lock-in a loan interest rate.

(3) Whether the loan contains a variable interest rate or balloon payment feature.

(4) Whether the loan includes a prepayment penalty.

(5) Whether the loan has a negative amortization feature.

(ii) The information to be disclosed under this subsection (b) shall be deemed to be disclosed, or redisclosed when required under subsection (c) hereof, when placed in first class mail to the applicant within the time specified, or when provided by personal delivery, overnight delivery, facsimile, email or other electronic means within the time specified. The applicant shall be requested to sign and return a copy to the licensee providing the disclosure, but failure by the applicant to do so as requested shall not be deemed a violation hereof. Refusal of an applicant to sign a copy of the disclosure received, however, shall be deemed sufficient grounds to refuse to close the loan transaction. In cases where a licensee with direct contact with an applicant is not the licensee providing the loan, it shall not be necessary to duplicate the disclosures, nor any redisclosures that may be required hereunder, and any disclosure or redisclosure by one of such licensees shall be deemed compliance herewith."

The primary purpose of these proposed changes is to attempt to avoid what would be a duplicative disclosure in almost every case. In virtually 100% of broker situations, the lender will not have determined each of the 5 characteristics required to be disclosed within 3 days of receiving the application. In a very substantial number of non-broker applications – perhaps approaching 100% also – the lender will not have determined each of the terms of the loan as listed, as those terms will be subject to review and confirmation of information on the application, and subsequently in many cases, negotiation with the applicant. Therefore, what is suggested is a disclosure that shows the applicant the terms that will be disclosed, but not the decisions made with regard to them in the initial disclosure. Subsequently, when all of those terms are known, then an individualized disclosure can be made.

While this still requires duplicative disclosures, the initial disclosure will not need to be individualized, but can be a standard disclosure in cases where only some of the required disclosure items have been determined within 3 days after the application is received.. This will alert the applicant that those items will be disclosed; will help reduce unnecessary expense; reduce confusion on the part of applicants (who will not have to retain two disclosures with partial disclosures on each); and reduce errors which will almost certainly result when some of the disclosures are made at one time and some at a later time.

CLARIFICATION OF REDISCLOSURE REQUIREMENT

"§46.2(c) *Required redisclosures.* A licensee who has issued the disclosure form required by subsection (b), or the licensee who shall be providing the loan, shall issue an updated disclosure form at the time the such licensee knows or reasonably should know that the initial disclosure form is inaccurate, or that an item determined at the time of the initial disclosure has since been changed, either by request of the applicant or by discovery of additional relevant information or for any other reason. The redisclosure shall advise the applicant as to the changed provision and shall indicate that the others remain as originally disclosed. In either case, redisclosure by one licensee shall be sufficient hereunder, and the provisions of subsection (b)(ii) shall apply to such redisclosure."

If the changes suggested for subsection (b) are adopted the applicants will be given one disclosure with all of the substantive provisions decided, either as the initial disclosure, or after a disclosure which simply says that the items will be disclosed at a later date. A redisclosure would then be required only if changes are made to one or more of the 5 items disclosed. The last sentence would try to clarify that the same disclosures should not be required of both a broker and lender, to try again to reduce expense, confusion and mistakes.

CLARIFICATION OF ABILITY TO REPAY PROVISIONS

"§46.2(e) *Evaluation of applicant ability to repay.*

(1) A licensee shall not offer a covered loan without having reasonably determined, based on the documents and information provided under this subsection, that the applicant will have the ability to repay the loan in accordance with the loan terms and conditions by final maturity at the fully indexed rate, assuming a fully amortized repayment schedule. The requirement to assume a fully amortized repayment schedule shall not be deemed to prohibit balloon mortgages.

(2) In performing an analysis to determine whether an applicant will have the ability to repay a covered loan, a licensee shall consider, verify and document

(i) the income of the applicant.

(ii) fixed expenses of the applicant. For purposes of this subsection, fixed expenses shall mean the monthly principal and interest on the loan and the taxes and insurance on the mortgaged premises, whether such taxes and insurance are escrowed or not.

(3) A licensee may consider and document information in addition to verified income and fixed expenses as required in subsection (e)(2) in determining an applicant's ability to repay an offered loan, provided that the additional factors are reasonably related to an applicant's ability to repay.

(4) A licensee shall not primarily rely upon the sale or refinancing of an applicant's collateral in determining an applicant's ability to repay an offered loan.

(5) All records, worksheets, and supporting documentation used in the licensee's ability to repay analysis shall be maintained in the applicant's loan file, if a loan is consummated, for the same period as the loan records are required to be maintained.

(6) In determining an applicant's ability to repay a loan offered under this subsection, a licensee shall not ignore facts or circumstances that it knows or reasonably should know which would indicate that an applicant does not have the ability to repay the offered loan.

(7) In addition to the analysis required by this subsection, great weight and due consideration shall be given to the Guidance on nontraditional Mortgage Product Risks, as amended, issued by the Department in establishing a licensee's internal procedures and guidelines when implementing the ability to repay analysis required by this subsection.

(8) This subsection (e) shall have no application to FHA streamline refinance loans, FHA insured HECM reverse mortgage program loans, or workout arrangements on existing loans related to actual or threatened default, which may or may not include additional loan obligations, or other loans where federal or state regulations indicate that obtaining of the current income status of the borrower is not required of the lender."

While the PFSA understands the concern that loans may be made to sub-prime applicants without adequate consideration of their circumstances, we do not believe that this warrants the verification and documentation of the income and fixed expenses of every applicant. Accordingly we recommend adding the reference to "covered loans". In many cases, prime loan candidates can be selected properly with automated systems which capture relevant information based on credit scores and other information, but do stop short of verifying income and "fixed expenses". If the "ability to repay" requirement is imposed on all applicants of licensees – as opposed to the "covered loan" or subprime category, where the real problem apparently lies - this will create a significant disadvantage in their ability to compete for prime customers since federally regulated competitors will not have this same requirement.

We have added a definition of "fixed expenses" as the monthly amounts due under the mortgage for principal and interest, plus the taxes and insurance on the property, whether

escrowed or not. Without a definition, it will be impossible to guess what "fixed expenses" might mean in any given case.

In addition, there are certain types of loans, such as FHA insured "streamline" loans and reverse mortgages for seniors where consideration of the current income status of the borrower is not required or is limited. The proposed language would appear to effectively preclude licensees from participating in such programs, and they should be excluded here, and in subsection 46.2(f)(3), as noted below.

Lastly, we believe that subsection 46.2(e)(1) could be interpreted to prohibit balloon mortgages by the reference to "fully amortized repayment schedules". We do not believe any reason exists to prohibit balloon loans and suggest language to avoid that interpretation.

PROPOSED CHANGES TO LOAN TRANSACTION PROHIBITIONS

"§46.2(f) *Loan transaction prohibitions.* A licensee may not:

(1) Advise or imply to an applicant that the applicant's income is not relevant to the loan transaction.

(2) Recommend or imply that an applicant default on any existing contract or financial obligation.

(3) Advise or induce an applicant to refinance an existing loan or otherwise enter into a new financial obligation without performing the ability to repay analysis required by subsection (e). Provided however, that this subsection shall have no application to FHA streamline refinance loans, FHA insured HECM reverse mortgage program loans, or workout arrangements on existing loans related to actual or threatened default, which may or may not include additional loan obligations, or other loans where the licensee has not initiated the request for the refinancing, but the request has come from the borrower.

(4) If an applicant qualifies for a loan offered by the licensee, other than a covered loan, offer to the applicant a covered loan without advising the applicant that the applicant qualifies for a loan other than a covered loan.

(5) Advise or imply that an applicant should ignore any required disclosures or suggest that a document or the execution of any document is unimportant or of no consequence.

(6) Direct, encourage, permit or otherwise be involved with the improper execution of any document, including:

(i) Requesting or allowing an applicant to sign documents that contain blank spaces where material information regarding the loan transaction is required.

(ii) Permitting the execution of documents where signatures are required to be witnessed without the witnesses being physically present.

(iii) Permitting someone other than the required signatory to execute a document unless otherwise authorized by law.

(7) Knowingly submit or permit or encourage an applicant or third party to submit, false or misleading information, or information that the licensee reasonably should know is false or misleading, to any party to a loan transaction.

(8) Improperly influence, or attempt to improperly influence:

(i) An appraiser by committing any act or omission that is intended to:

(A) Compromise the independent judgment of an appraiser.
(B) Ensure that an appraisal matches a requested or target value.

(ii) Any other entity related to the mortgage loan business, such as notaries, title companies, real estate agents, builders and sellers of properties.

(9) Obtain insurance required for a loan for an applicant at loan consummation without providing the applicant with the opportunity to secure or provide evidence of their own insurance.

(10) Charge an applicant a fee for any legally required notices or disclosures unless otherwise authorized by law.

(11) Pay compensation to or receive compensation from, contract with, or employ any person engaged in the mortgage loan business who is not licensed or otherwise exempt from licensure.

(12) Render legal advice to an applicant <u>provided that providing disclosures or other documents required under this regulation, or providing information as to the content of this or other department regulations, or advising applicants of the acts and information required to satisfy the lender's requirements in order to close a loan shall not be deemed to be providing legal advice."</u>

The suggested change to subsection 46.2(f)(3) is necessary to permit lenders to participate in FHA streamline loans and reverse mortgages. Federal statutes controlling such loans permit refinancing without the normal checking of income and other items such as appraisals, and in the case of reverse mortgages of course, the borrower makes no payments and the property is considered as the sole source of repayment. Federal competitors will be able to participate in such transactions at a significantly lower cost to the applicant than could licensees if the requirements of documenting income are applied to Pennsylvania licensees. A change is also proposed in subsection 46.2(e)(8) above, using similar language.

With regard to subsection 46.2(f)(12), since there is no definition of rendering legal advice provided, we feel it is necessary to state that the licensee, in doing what is required of him or

her under the regulation, or in advising as to what is needed to obtain the loan, is not providing legal advice – at least as far as the Department of Banking is concerned.

CLARIFICATION OF FUNDING RULES

§46.2 (g) *Loan funding.*

(1) A licensee lender may not refuse or fail to fund a consummated loan, other than when an applicant rescinds the loan in accordance with 12 CFR 226.15 or 226.23 (relating to the right of rescission), as applicable.

(2) A licensee lender shall fund a consummated loan in a reasonable time period after consummation of the loan or in accordance with any commitment or agreement with the applicant; provided that, if an applicant has a right of rescission under 12 CFR 226.15 or 226.23 (relating to the right of rescission), a licensee lender is not required to fund a consummated loan in accordance with this subsection until after the applicable recession period has ended.

(3) Any post-closing underwriting or quality control review conducted by a licensee lender after the consummation of a loan shall not delay the funding of a loan or result in a failure or refusal to fund the loan in accordance with the provisions of this subsection, unless such underwriting or quality control review discloses facts that (i) were falsified or misrepresented by the borrower, or (ii) that have changed subsequent to the consummation of the loan, but prior to funding, and that would have caused the lender to deny the loan if such facts were known prior to consummation of the loan.

(4) Except as provided in subsection (g)(3), a licensee shall disburse loan funds in accordance with any commitment or agreement with the applicant.

(h) *Licensee responsibility to provide documents.* A licensee shall provide to an applicant or authorized representative of an applicant, upon request of the applicant or authorized representative of the applicant, and unless prohibited by federal or state law, copies or originals of the documents associated with a loan that an applicant has paid for or signed, such as loan applications, appraisals, surveys, loan documents, disclosures and any fee agreement executed by the applicant and the licensee. Provided however, that this shall not relieve the licensee from delivering to the applicant or authorized representative of the applicant, all documents that are required by law or regulation to be delivered.

(i) *Payoff statement or statement of mortgage reinstatement.* A licensee lender shall provide a borrower with payoff statements or statements of mortgage reinstatement, as applicable, for the borrower's loan within 7 business days of receipt of a written request by a borrower or a person authorized by the borrower."

The suggested language would permit a lender to delay or refuse to fund a loan where fraud or other misrepresentation is discovered after the closing but prior to the funding. This is certainly a reasonable limitation on the requirement for prompt funding, and it does not simply

let the lender unilaterally change credit standards or otherwise simply decide not to fund the loan.

The added language to subsection (h) would not require a licensee to deliver appraisals or surveys unless requested by an applicant, but would, of course, require all loan documents now required by law or regulation to be provided to the applicant or the authorized representative.

CONCLUSION

We believe the changes suggested do not do any harm to the primary intention of the proposed regulation. In that regard, we agree that early disclosure of the 5 items listed in subsection 46.2(b) will be positive. In particular, we feel two of the disclosures are most important. They have been mentioned many times by consumer advocates – and are (1) the disclosure of whether a prepayment penalty will apply and (2) whether the taxes and insurance on the property will be escrowed by the lender, or not. We have heard, many times, that borrowers who said they were not aware of those factors ended up feeling as though they had been misled by lenders, and as a consequence were in trouble with regard to a loan. Although it is not clear that lenders have misrepresented any of those items, and there may be many reasons for the problems borrowers suffer, we agree that those items should be clearly disclosed.

As noted, we do not believe that our suggested changes harm the intent of the regulation in that regard in any way, but will help reduce costs, confusion and mistakes, and will help ensure that credit is available to those who want and need it.

Sincerely,

David B. Ward