July 28, 2009

Maine Bureau of Financial Institutions
Maine Bureau of Consumer Credit Protection
Joint Advisory Ruling #117
The Conforming Law and its effect on previous Joint Advisory Rulings and the Tangible Net Benefit and Ability to Pay Rule

Dear:

Due to the recent passage of LD 1439 (now Public Law 362), "An Act To Conform State Mortgage Laws with Federal Laws," significant changes have been made to Maine's anti-predatory lending laws. Following the passage of Maine's anti-predatory lending laws in 2007 and 2008, the Bureaus issued a number of advisory rulings and promulgated a joint rule regarding the "tangible net benefit" and "ability to pay" analyses. In light of the passage of "An Act to Conform State Mortgage Laws with Federal Laws," you have asked the Bureaus to clarify whether, and the extent to which, the advisory rulings and joint rule in relation to Maine's anti-predatory lending laws still apply.

The guidance in this advisory ruling is effective as of June 11, 2009, except that the new rate thresholds, using the "average prime offer rate" as determined by reference to 12 CFR 226.35(a) (found in the definition of "rate spread home loan" in section 8-103(1-A)(V) of the conforming law) become effective on October 1, 2009.

AR # 110 - Request for Guidance regarding "odd days'" or "per diem" interest

Conclusion reached by the Bureaus in AR # 110: "Per diem" or "odd days'" interest is not to be included when calculating "points and fees" as that term is defined in 9-A 8-103(1-A)(U).

Analysis: The definition of "points and fees" was repealed and replaced by a new definition in "An Act to Conform State Mortgage Laws with Federal laws." The new law references only one section of Reg Z, 226.32(b)(1), without referencing 226.4, and also includes prepayment fees and penalties. AR # 110 references the language found in section 226.32 and also references the Official Staff Commentary relating to section 226.32 that interest including per diem interest paid at closing is not a 'point or fee' for section 226.32 purposes. Therefore, the conclusion reached by the Bureaus that "per diem" or

odd days' interest is not to be included when calculating "points and fees" remains unchanged.

AR # 111 - Exclusion of HELOCs from definition of "subprime loan"

Conclusion reached by the Bureaus in AR # 111: HELOCs are not subject to the "ability to pay" underwriting requirement of 9-A M.R.S.A. section 8-103(1-A)(BB) and section 8-206-D(1)(G) except to the extent a HELOC is a Simultaneous Second-Lien Loan as defined in the "Interagency Guidance on Nontraditional Mortgage Product Risks" or meets the criteria of a high-rate, high-fee mortgage under s. 8-103(1-A)(V).

Analysis: "An Act to Conform State Mortgage Laws with Federal Laws" repeals the term "subprime mortgage loan" and creates a new term, "higher-priced mortgage loan." As with a "subprime mortgage loan" a "higher priced mortgage loan" means either a residential mortgage loan that is a "nontraditional mortgage" as described in the Interagency Guidance on Nontraditional Mortgage Product Risks or a "rate spread home loan." Loans that fit the definition are subject to additional consumer protection provisions, including ability-to-pay analysis.

On October 1, 2009 a component of the definition of "higher priced mortgage loan" will change such that "rate spread home loans" will be comprised of "high rate, high fee" loans and loans falling under the new federal definition of "higher priced mortgage loans" as set forth in 12 C.F.R. 226.35(a). The Bureaus note that, while the new federal definition of "higher-priced mortgage loans" contemplates loans secured by first and subordinate liens, HELOCs are specifically excluded from the "higher-priced mortgage loans" definition.

Because HELOCs are specifically excluded from the new federal definition of "higher-priced mortgage loans" and HELOCs are expressly excluded from the definition of "nontraditional mortgage," certain HELOCs will continue to be exempt from the requirement to perform ability-to-pay analysis. The Bureaus conclude that HELOCs should not be included in Maine's definition of "higher-priced mortgage loan" except to the extent that a HELOC is a Simultaneous Second-Lien Loan as defined in the Interagency Guidance on Nontraditional Mortgage Product Risks, or meets the criteria of a high-rate, high-fee mortgage.

Note: Certain Simultaneous Second-Lien Loans known as "convenience" HELOCs are excluded from the definition of "nontraditional mortgage" if they meet the requirements set forth in AR # 116. As set forth in the "Interagency Guidance for Nontraditional Mortgage Product Risks," a "nontraditional mortgage" is a mortgage containing an interest or principal deferral attribute.

AR # 112 - Computation of "Total Loan Amount"

Conclusion reached by the Bureaus in AR # 112: Assuming the loan documents do not contradict this characterization, loan proceeds are applied first to the transaction being financed, second to any points and fees, third to any excludable costs and fourth to cash out to the borrower.

Analysis: The definition of "total loan amount" in the new law remains unaltered. Although the definition of "total loan amount" references "points and fees," a term which has been altered by the new law, there is no basis for altering the order of allocation of loan proceeds as set forth in AR # 112. The order of allocation set forth in AR # 112 remains unchanged.

Bureaus' Joint Rule: Guidelines for Determining Reasonable Tangible Net Benefit and Ability to Pay -- the "Ability to Pay" provisions of the Joint Rule

Analysis of "ability to pay" provisions of the joint rule: The joint rule's "ability to pay" section was based upon a provision in "An Act to Protect Maine Homeowners from Predatory Lending" passed in 2007, that has since been amended twice by the Maine Legislature. Most recently, the "ability to pay" provisions in Maine law have been repealed and replaced in "An Act To Conform State Mortgage Laws with Federal Laws," in which the new "ability to repay" provisions are modeled after federal language. This new federal language is different than the original "ability to pay" language in previous Maine law and includes highly specific criteria for determining ability to repay. Because the original "ability to pay" language in previous Maine law, upon which the "ability to pay" provisions of the joint rule were based, has been repealed, the "ability to pay" provision of the joint rule is no longer effective. Therefore, creditors should no longer seek guidance from the "ability to pay" provision of the joint rule but, rather, from the new "ability to repay" provision in Maine law, as enacted by "An Act To Conform State Mortgage Laws with Federal Laws."

AR # 113: "Ability to Pay" under the Bureau's Joint Rule: Guidelines for Determining Reasonable, Tangible Net Benefit and Ability to Pay

Conclusion reached by the Bureaus in AR # 113: The joint rule's "ability to pay" section requires a creditor to consider both secured and unsecured debt payment in calculating ability to pay, but permits that creditor to rely on reported monthly payments to other creditors. The Bureaus will not require creditors to attempt to "fully index" payments that may be due to other creditors in the future.

Analysis: The Bureaus note that, according to the Official Staff Commentary to the new federal "ability to repay" provisions in Regulation Z, upon which our new state’s law is based, a credit report may be used to verify an obligation that a borrower has listed on an application. The Official Staff Commentary notes that a credit report may not reflect an obligation that a borrower has listed on an application and that, "the creditor is responsible for considering such an

obligation, but the creditor is not required to independently verify the obligation." Although the "ability to pay" provision of the joint rule, upon which AR # 113 delineates, is no longer effective, creditors may continue to rely upon the conclusion reached by the Bureaus in AR # 113 to the extent that a creditor is required to consider both secured and unsecured debt in calculating repayment ability and may rely on reported monthly payments to other creditors. However, creditors will only be afforded the "presumption of compliance" if the underwriting procedures specified in federal Regulation 226.34(a)(4)(iii) are followed. The Bureaus will continue to look to federal guidance for interpreting the new "ability to repay" provisions now in Maine law in an effort to maintain conformity between Maine and federal law.

Bureaus' Joint Rule: Guidelines for Determining Reasonable Tangible Net Benefit and Ability to Pay -- the "Tangible Net Benefit" provisions of the Joint Rule, and AR # 114

Background: As mandated by "An Act to Protect Maine Homeowners from Predatory Lending," enacted in 2007, the Bureaus promulgated a joint rule in late December 2007 providing guidance for determining whether or not a borrower receives a "tangible net benefit." In "An Act Relating to Mortgage Lending and Credit Availability," enacted as emergency legislation in early January 2008, the prohibition against "flipping" was narrowed to apply only to instances when a creditor extends a subprime mortgage loan to a borrower. On January 17, 2008, the Bureaus accordingly issued AR # 114 clarifying the "tangible net benefit" provision of their joint rule applies only when making subprime mortgage loans, and also attached a revised "tangible net benefit form" incorporating revisions to the form to reflect this change.

Analysis: Following passage of "An Act To Conform State Mortgage Laws with Federal Laws," the prohibition against "flipping" still exists. However, because the definition of "subprime mortgage loan" has been repealed and replaced by "higher priced mortgage loan," the tangible net benefit analysis in the joint rule now applies when a creditor makes a "higher-priced mortgage loan." Thus, the tangible net benefit provisions of the joint rule, AR # 114, and the tangible net benefit form should now all be read substituting "higher-priced mortgage loan" for "subprime mortgage loan."

AR # 115 - Treatment of Construction-to-Permanent Loans

Conclusion reached by the Bureaus in AR # 115: Construction-to-permanent mortgage loans may be residential mortgage loans but are not subprime mortgage loans. However, this conclusion applies only in those cases in which: (a) the only "subprime" attribute of the "construction phase" of such loans is the payment of interest only during this phase; and (b) there are no "subprime" attributes to the "permanent phase" of these loans.

Analysis: In coming to their conclusion in AR # 115, the Bureaus determined that construction-to-permanent loans were not contemplated in the "Interagency Guidance on Nontraditional Mortgage Product Risks." Like the old definition of "subprime mortgage loan," the new definition of "higher priced mortgage loan" includes "nontraditional mortgages" defined by reference to the Interagency Guidance. Therefore, the conclusion reached by the Bureaus that construction-to-permanent loans are not subprime mortgage loans, provided that the only "subprime" (or now, "higher priced") attribute of these loans is the payment of interest only during the construction phase, remains unchanged with respect to higher-priced mortgage loans.

AR # 116 - "Convenience HELOCs

Conclusion reached by the Bureaus in AR # 116: Those "convenience" HELOCs that permit deferral of payment of principal or interest should not be treated as "simultaneous second-lien loans" under the Interagency Guidance and, therefore, will not be considered "subprime mortgage loans" under Maine's Predatory Lending Law. A simultaneous second-lien HELOC shall be regarded as a "convenience" HELOC under the Interagency Guidance, if (1) the convenience HELOC is not drawn at closing (or at the end of any applicable rescission period) to satisfy the first mortgage lender's equity requirements for granting the first mortgage loan, or to avoid payment of private mortgage insurance; and (2) the combined loan to value ratio of the first residential mortgage loan and the line amount of the second lien "convenience" HELOC is 90% or less.

Analysis: In coming to their conclusion in AR # 116, the Bureaus determined that the "Interagency Guidance on Nontraditional Mortgage Product Risks" is primarily concerned with those simultaneous second-lien loans that significantly reduce owner equity and increase credit risk. The Bureaus further recognized that, if reasonable equity levels exist and the "convenience" HELOC is not used toward the down payment or to avoid payment of private mortgage insurance, then these types of loans lack the negative qualities that the Interagency Guidance seeks to address.

The Bureaus remain of the view that, if the conditions set forth above are met, then these types of loans should not be treated as "simultaneous second-lien loans" under the Interagency Guidance and, therefore, will not be considered a "higher-priced mortgage loan." The conclusion reached by the Bureaus in AR # 116 remains unchanged, except that it should be read substituting "higher priced mortgage loan" for "subprime mortgage loan."

Sincerely,

/s/ Lloyd P. LaFountain III

Sincerely,

/s/ William N. Lund

Superintendent

Bureau of Financial Institutions

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