LEGISLATIVE PROPOSALS TO ADDRESS PREDATORY LENDING PRACTICES IN MAINE

State of Maine
Office of Consumer Credit Regulation

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1. Introduction

During the summer and fall of 2006, in response to a request from the office of Governor Baldacci, the Maine Office of Consumer Credit Regulation (OCCR) conducted a study of predatory mortgage lending practices in Maine. This report summarizes the results of that inquiry, and suggests preventive legislation.

To elicit public comment and to assist commenters to focus their suggestions on specific topics arising from lending activities affecting Maine consumers, the OCCR drafted a document titled "Request for Public Comment", and a 23-page compilation of issues brought to the attention of state mortgage regulators in recent years. That document posed twenty-seven questions in areas ranging from loan officers' use of prescreened leads in their telemarketing sales pitches, to rate locks, to changes in terms at closing, to servicing issues and prepayment penalties.

The general public and the industry were invited to an "Opportunity for Public Comment" in the offices of OCCR on Monday, the 11th of September, 2006, and testimony was presented for more than 6 hours. Participants were invited to submit written comments at the meeting and for a week after the close of testimony.

More than 30 interested parties attended the hearing. Ten groups submitted oral testimony, ten sets of written comments were received, and several commenters subsequently followed up initial written submissions with supplemental materials.

2. Summary of Findings and Recommendations

Some of the most significant features of this report are the legislative action steps that OCCR is *not* recommending be taken. For example, the agency does not urge the Legislature to try to determine a way to "force" national banks to comply with state lending laws. Regulatory authority over national banks, for all intents and purposes, is no longer available to states. Absent a major reversal of the preemptive trend via a state-favorable ruling in the pending U.S. Supreme Court case of *Wachovia v. Waters*, it seems unlikely that state monies would be well spent at this time in an effort to overturn the interpretations and regulations of federal bank regulators and the federal court decisions that have nearly-unanimously supported those federal regulatory interpretations and regulations.

Likewise, issues such as whether to regulate independent settlement agents, whether to incorporate a "net tangible benefit" test for mortgage loans, and whether to hold secondary market purchasers liable for mistakes of the original lenders, raise too many implementation questions to be properly addressed in the relatively short timeframe encompassed by this study and report.

At the opposite end of the spectrum, several OCCR proposals met with the approval of the vast majority of commenters, at least conceptually. These include quite progressive measures, such as the recommendation to incorporate the federal Real Estate Settlement Procedures Act (RESPA) into state law.

Between the extremes of unreachable goals and unanimous consent are proposals on which reasonable advocates could and did disagree, consistent with the historic positions of the interest groups they represent. Those issues posed the most challenging decisions for OCCR, and likely resulted in what will be the most controversial recommendations.

Among these proposals is the suggestion that the "points and fees" trigger that subjects a mortgage loan to the protective provisions of Maine's high-rate, high-fee loan laws, be lowered from the current level of 8% of the loan total, to a new threshold of 5%. Lenders in states such as Massachusetts and Connecticut are already operating under this level of stricture.

A final category of legislative proposals derives not from specific questions posed in OCCR's original Request for Public Comment, but rather from input from interested parties who responded to Question # 27: "What other steps (not addressed in this request) could Maine take to address predatory lending practices…?" For example, two national regulatory associations, the Conference of State Bank Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR) asked Maine and all other states to amend their laws to permit (but not require) participation in a multi-state mortgage lender licensing project, modeled after the nationwide registration system that helps state securities regulators keep track of broker-dealers and of investment products in the national securities market, and this report and the attached legislation incorporate that proposal.

This report follows the general format set forth in the August 30, 2006 Request for Public Comment. Topics are addressed in the order found in that earlier document, and input from interested parties is referenced where appropriate. The reader is told of the OCCR's recommendation on each issue, and for those issues for which legislation is recommended, that proposed legislation is described in the text, and is then compiled into draft legislative documents attached to this report as Appendix #1 and Appendix #2. The initial August 30, 2006 Request for Public Comment is also attached, for ease of reference, as Appendix #3.

Issue #1: Mortgage "trigger leads"

Trigger leads consist of information about mortgage applicants that is sold by credit reporting agencies to competitors of the company that accepted an initial application. Maine consumers have complained to the OCCR that they were confused to receive solicitations from companies other than "their" lenders, and they report that they could not understand how telemarketers knew, often within a day or less, that the consumers had just applied for a mortgage loan.

Concerns evaluated by the OCCR included 1) that too much personal financial information about consumers was being given to subscribers of mortgage trigger lead services; 2) that the telemarketers were not complying with the federal laws' requirements to provide the consumer with a "firm offer of credit"; 3) that the law requiring that consumers be told of their opt-out rights to avoid prescreened solicitations, did not contemplate telephone solicitations, only written ones; 4) that callers were misleading consumers, by omission or commission, with respect to the callers' identity, or about how the information concerning the consumers' recent application was obtained ; and 5) that callers were enticing consumers to drop "their" lenders with promises of lower rates and fees, only to subsequently raise those rates and fees (*i.e.*, they were employing "bait and switch" tactics).

Several developments have changed the landscape of this issue since the initial Request for Comments was issued in late August, 2006. First, publicity generated around this activity has almost certainly caused credit reporting agencies to tighten their requirements on users of prescreened trigger leads. Second, the OCCR had an opportunity to carefully review § 604(c)(2)(1)(B)(C) of the Federal Fair Credit Reporting Act, and noticed a large potential loophole with respect to the issue of how much detailed information a credit reporting agency can sell to a trigger-leads subscriber. The federal law states that a subscriber can receive a consumer's name and address, a non-unique identifier for internal record-keeping, and "other information pertaining to a consumer that does not identify the relationship or experience of the consumer with respect to a particular creditor or other entity." Credit reporting agencies can (and have) argued that this provision permits the sale of the most detailed financial information, so long as the names of the creditors to which the debts are owed, are not revealed.

The final development is a review of the federal laws preemptive provision, found in §625 of the federal FCRA. Under the heading "Relation to State Laws", the federal act preempts any "requirement or provision . . . under the laws of any State . . . with respect to any subject matter regulated under . . . subsection c . . . of section 1681b of this title, relating to the prescreening of consumer reports . . . ." To survive a challenge based on preemption, therefore, a state law must be general in scope rather than specific to prescreened procedures, and should likely be based on that state's unfair trade practices laws.

The OCCR believes this issue will continue to pose serious problems in this State and all other states, and that we are just beginning to see prescreening sales practices and problems in their infancy. While the federal preemptive language, we believe, prevents a state from prohibiting or severely restricting legitimate use of such trigger leads, in our opinion it is within a state's prerogative to require that such information be utilized in a way that conforms with federal law and that is not misleading to consumers. Therefore, the attached bill proposes enactment of a new section, § 1327-A of 10 MRSA (*see* Sec.

11 of the proposed legislation, attached as Appendix #1), that prohibits misleading or non-compliant use of trigger leads.

Issue #2: Loan broker as non-agent of the consumers

Question #2 of the Request for Comment asked whether a loan broker should be required to disclose that he or she is not the agent of the consumer. While the OCCR had hopes of proffering a simple solution to this issue, what we discovered is that this issue was more complex than initially anticipated.

Our original goal was laudable; namely, to make certain that a consumer knew not only that a loan broker is an independent contractor who may not always have a duty to act in the best interest of the consumer, but that actually the system of lenders paying brokers "yield spread premiums" can create the result that the broker acts in a manner directly at odds with the consumer's interests, at least to the extent that the consumer hires a loan broker to obtain a loan at the lowest rate.

However, what we learned from interested parties is that common law may assign certain duties to a loan broker to act in good faith toward the consumer, and that if Maine law were amended to require a non-agency disclosure, it might operate as a "release", permitting the loan broker to escape a common-law duty to act in good faith.

So while OCCR has decided not to recommend that all loan brokers be required to provide a non-agency disclosure, our recommended legislation *does* contain a provision requiring that loan brokers disclose in writing, as part of their initial contract, the amount they will receive from the lender (*i.e.*, the yield spread premium). *See* Section 8 of the bill attached as Appendix 1, which amends the required contract to include disclosure of payment "by the consumer <u>or by any other person or entity</u>." In addition, through law amendment, rule or compliance exam guidelines, OCCR intends to curtail a recent industry tendency to list a vague, wide range of commissions on a loan broker contract; *e.g.*, "We will charge you a fee of between 1% and 5% of the loan for our services". On a $200,000 loan, this "range" means that a consumer could pay any amount between $2,000 and $10,000 as a broker fee. That type of nonspecific estimate would not pass muster in the world of car repairs or house renovations, and in our opinion it should not be tolerated in the mortgage-brokerage business.

Issue #3: Do federally regulated lenders make predatory loans?

In the Request for Public Comment, we asked commenters to opine on the extent to which federally–chartered banks, or their subsidiaries that claim exemption from state laws, are involved in making predatory mortgage loans. We did not receive a great deal of input in response to the question. We believe this is a result of as many as four distinct factors. First, we believe that the vast majority of loans being made by banks and their subsidiaries in Maine are not high-rate, high-fee loans, and are therefore likely not “predatory” in the usual meaning of the word. Second, we believe that the direct or indirect oversight of federal regulators has been effective at discouraging the federally–regulated lenders from engaging in abusive tactics. Third, while there are certainly exceptions, as a rule federally–chartered lenders may make less use of loan brokers than do state-licensed, non-bank lenders, so that fact may help federal lenders avoid certain categories of predatory practices associated primarily with brokers. And fourth, commenters may feel, with some justification, that to engage in a debate about predatory lending by federal lenders is not a worthwhile expenditure of time, since as demonstrated by the string of recent court decisions preempting state regulation of those lenders, a state’s effort to control federal lenders’ activities would likely not survive a legal challenge by the lenders.

Although the OCCR did raise the question of state authority over federal banks, we have opted not to directly address the topic in the proposed legislation. Regulation of federal lenders is, for all current intents and purposes, outside the jurisdiction of the OCCR. To a great extent, such regulation is also outside the purview of the Maine Bureau of Financial Institutions, which is primarily empowered with authority to regulate state-chartered financial institutions.

Issue #4: Can Maine impose anti-predatory lending standards on federally-chartered banks and their subsidiaries?

Given the proclivity of federal bank regulators to assert, through interpretation and regulation, exclusive supervision of federal institutions, and taking into consideration the apparent willingness of federal courts to uphold those assertions and of Congress not to intercede, it is evident that if changes in Maine law are to affect national–bank lending, it will come about as an *indirect* result of state action rather than as a *direct* result. However, “indirect“ does not mean illusory, If a state law changes the behavior of state-licensed loan brokers and lenders, and changes the products they offer, the protection and benefits for consumers will likely flow over into national-lender practices. If loan broker activity is affected, to the extent that brokers arrange loans from nationally-chartered lenders, consumers will likewise benefit. And with respect to state vs. federal lenders, these two categories of business are locked into a very real competition, so consumers who comparison-shop for features and costs will reap the positive impact of state regulation, because federally-regulated lenders can be expected to amend their products and practices to remain competitive.

Therefore, as with Issue #3, above, the proposed legislation attached to this report is not designed to *directly* affect the lending practices of federally-regulated lenders; rather, the beneficial impact may flow from one set of entities to the other, to the net advantage of consumers.

Issue #5: Should anti-predatory lending laws apply to state-chartered banks and credit unions?

The attached proposed anti-predatory lending bill (Appendix #1), and the separate RESPA–related legislation (Appendix #2), constitute a combination of measures, some of which would affect both bank and non-bank entities (*e.g.*, incorporation of RESPA into state law, and the lowering of the 8% "rates and fees" threshold for high-cost loans to 5%), and others of which would exclusively affect non-bank lenders and loan brokers (*e.g.*, the proposed changes to Article IX of the Consumer Credit Code, found in Sections 4 through 7 of the bill, that would apply only to non-bank lenders). This reflects the OCCR's view that while some overriding principles, such as incorporation of RESPA, should be applied broadly, the more detailed issues such as the rate-lock provisions and the proposals regarding the form of the loan contract in describing pre-payment penalty provisions, should be left up to each agency (OCCR for non-banks, and the Bureau of Financial Institutions for depository institutions) with respect to such provisions or their enforcement. The OCCR is hopeful that the state-chartered financial institutions will not request blanket exceptions from all provisions of these bills, since 1) the mortgage lending models (if not the practices) of many banks are not substantially different from those of non-banks, nor are the product offerings, forms, and intended secondary market recipients; and 2) to permit exclusion of the banks would be to lose valuable legal and advocacy resources that will help to positively shape the legislative proposals resulting from this report, as well as the implementation and enforcement of any laws resulting from this study.

Issue #6: OCCR's Rule 250 – Alternative Mortgage Transactions

OCCR's "Rule 250" governs the making of "alternative" mortgage transactions, a description defined to primarily include those mortgage loans featuring an interest rate that adjusts upward or downward in tangent with an outside index, and those loans that contain a large single payment ("balloon") at the end of the loan term.

Rule 250 exempts from certain of its provisions loans made to conform to the secondary loan market underwritten by the quasi-government entities Federal Home Loan Mortgage Corporation (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac) and Government National Mortgage Association (Ginny Mae). However, those are not blanket exemptions, and certain of the rule's provisions, such as the requirement that no loan's initial term may extend beyond 31 years, apply even to these so-called "federally-related" loans. In OCCR's Request for Public Comment we asked whether some aspects of Rule 250 should be changed to permit additional loan products to be offered in Maine, if 1) those loan products are not associated with predatory lending practices; and 2) the products have found a ready market not only in other states, but here in Maine when offered by lenders (such as national banks and their affiliates) that are not subject to state law nor to Rule 250.

After receiving input from interested parties, OCCR has determined to proceed during the winter and spring months of 2006-2007 to repromulgate Rule 250 to consider accommodating a wider range of loan products. In any review of predatory lending practices, it is important that state regulators demonstrate a willingness to review past steps taken to protect consumers, and to liberalize those prior restrictions if it can be demonstrated that permitting Maine-regulated lenders to offer the same products as are offered by federally-regulated lenders will not increase the chances of incidents of predatory lending. In our experience, predatory lending often relates more closely to the sales practices utilized to market a product and the up-front costs of obtaining access to a product, than to the terms of the product itself.

The details of a new proposed rule need not be developed as part of this study. Rather, a draft rule will be issued for public review and comment through the usual Administrative Procedures Act rulemaking process, and interested parties will have the opportunity to respond with written submissions and (if a hearing is scheduled) through oral testimony.

Issue #7: Notice to loan broker customers about the effect of obtaining credit from a nationally-regulated lender

In its Request for Public Comment, the OCCR asked whether loan brokers who arrange credit with a nationally-regulated lender should be required to notify consumers that the resulting loan products would not be subject to the protections of Maine law, and that if the consumers had problems, the consumers would be required to seek help from distant federal regulators, rather than from regulators at the state level.

After reconsideration of this concept, and after review of the comments from interested parties, OCCR has decided not to pursue this idea of "warning" national-bank customers of the lack of state-level protections available to them. Rather, any such awareness campaign should likely focus on notifying consumers of the specific provisions of their loans (balloon features; mandatory arbitration clauses; prepayment penalties), regardless of the lender involved.

Issue #8: Should lenders and brokers be expressly prohibited from falsifying data on a consumer's application, or assisting in that falsification?

Current state and federal law prohibit consumers from falsifying information on an application for credit, but in general those laws do not apply to situations that consumers tell us occur not infrequently -- the tutoring of consumers by brokers and lenders on how to improve their chances at credit approval through omission or commission of information on an application, or the insertion of false information by the loan officer, even without the knowledge of the consumer.

Response to the proposal to expressly prohibit falsification by loan officers was strongly positive, both from the lending/brokering industry and from consumer advocates. Therefore, such provisions have been included in the bill, attached as Appendix #1, with respect to lenders (*see* Section 5 of the proposed bill) and loan brokers (*see* Section 9 of the proposed legislation).

Issue #9: Avoiding undue influence on appraisers by large lenders

As in the case of Issue #7, above, the problem of large lenders and brokers using their market power to pressure appraisers into "bringing up" their appraised values in order to support large loans, proved to be beyond the scope of this report and draft legislative language. It's not that the problem does not exist: it clearly does, and as was mentioned in the Request for Public Comment, it was one of the primary focuses of the recent *Ameriquest* multi-state settlement, which calls for appraisers on future Ameriquest loans to be selected randomly from a pool of qualified appraisers.

Rather, any such step would be very difficult to implement in Maine, where lenders and loan brokers have established working relationships with certain appraisers over the years, and where neither lenders and brokers nor appraisers want to be told that such relationships cannot be continued.

Instead, since providing an unwarranted, inflated value is a violation of appraisers' sworn ethical duties to produce valuations based exclusively on objective factors, all parties to the anti-predatory lending debate will have to rely upon the professionalism of appraisers, and on the unity of the appraisal industry to speak out and stand together if incidents of undue market influence occur, to prevent those incidents from recurring.

Issue #10: "Truth-in-Rate Locks"

Especially in times of rising interest rates, state regulators receive complaints from consumers regarding rate locks that expire, costing consumers the value of the anticipated rates. Since so many factors can influence the scheduling of a closing date, and since it is often difficult to apportion "fault" in such cases, it is challenging for state regulators to prove that a delay beyond the rate lock period was not the consumer's fault. In fact, it is sometimes difficult to prove that the rate was ever in fact locked in.

The OCCR received some graphic input from an interested party on this issue. An experienced loan officer said that she had worked in two separate establishments in which lenders or brokers took fees from consumers to lock in a rate, but then retained the funds without actually acquiring a rate commitment from a lender or secondary market purchaser. The commenter stated that the loan officers "gambled" that rates would not go up, and if the rates did rise, the loan officers would put forth to the borrowers a fictitious reason why the loan could not be made at the promised rate, and would then arrange a loan at the higher rate.

The attached legislation (Appendix #1, in Section 6 for lenders and Section 10 for loan brokers) requires loan officers to use a consumer's rate-lock funds to actually lock in a rate, and to utilize good-faith efforts to close the loan within the specified lock-in period.

Issue #11: Incorporation of RESPA into state law

As set forth in the Request for Public Comment, the elements of the federal Real Estate Settlement Procedures Act (RESPA) have become so intertwined into the aspects of mortgage lending over which the State of Maine already has oversight, that it is difficult to defer enforcement of RESPA any longer. The overwhelming majority of commenters agreed with that evaluation, and so by separate bill (*see* Appendix #2, attached), the OCCR recommends that RESPA be incorporated into state law. This change will permit the state regulators to develop expertise in interpreting and administering RESPA, for the benefit of consumers, loan brokers *and* lenders.

The proposed legislation may be subject to some minor amendments during committee deliberation. For example, historically the Revisor's Office has closely reviewed efforts to incorporate federal law into state statutes, because of the question of the effect of subsequent amendments to the federal law and whether those changes do, or do not, automatically flow into state law. In addition, while it is the intent of OCCR to bring RESPA into state law together with the same authority and remedies as are contained in the federal statute, we will closely review the mechanics of such a process to determine what impacts (for example, establishment of private state causes of action where none exist in federal law) may accrue as the result of incorporation of the federal law into state statutes. It is not OCCR's current intent to create enhanced remedies at the state level, but only to make remedies available to state regulators and consumers that are parallel to those existing in federal law.

Issue #12: "Surprise" changes in loan terms at closing

A consistent consumer complaint in recent years is "surprise" changes in loan terms, conditions and costs presented to the borrower for the first time at or just prior to closing, putting the borrower in the untenable position of 1) rejecting the entire deal and starting the long process anew; 2) going through the process and then rescinding (for rescindable transactions); or 3) agreeing to the changes, and absorbing the higher costs or less-favorable terms and conditions.

Consumers also tell OCCR that it's easy for loan officers to assign some reason, actual or fictitious, for the change in terms: the loan officers have possession of, or access to, all relevant details of the current and past financial histories of the consumer, with all its blemishes.

However, identifying a problem and solving it are two different matters. For example, consumers have told OCCR that they are surprised, at closing or even several years later, to learn that their loan terms include a prepayment penalty. With respect to the addition of a prepayment penalty provision just before closing, current federal law already requires redisclosure to the consumer prior to closing if a "subsequent event" makes the previously-provided information "inaccurate"; *see* Regulation Z, § 226.17(f). Therefore, part of the solution is improved enforcement if investigation of consumer complaints leads to evidence of failure to redisclose.

However, we feel that additional clarification is needed on this point. To that end, the attached proposed legislation includes specific provisions to address the occurrence of surprise inclusions of prepayment penalties (*see* discussion in connection with Issues #13, #14 and #21, discussed below).

Issue #13: Disclosure of late addition of prepayment penalty

A consumer receives two separate documents within 3 days of application: a good faith estimate (GFE) pursuant to RESPA, that does not reference whether or not a prepayment penalty will be included in the final loan, and an initial Truth-in-lending disclosure, which *does* include a reference to whether or not a prepayment penalty will be a feature of the loan.

While it's clear that a material change from the GFE requires re-disclosure, no such specific requirement exists with respect to the Truth-in-lending disclosure. Certainly the final mortgage contract (note), or at least a rider (amendment) to that contract, will contain a reference to the penalty. However, consumers who have been subjected to the late addition of a prepayment penalty tell us they needed a more obvious flag to this significant change in terms.

For that reason, Section 3 of the proposed legislation (*see* Appendix #1) contains a specific requirement for redisclosure to consumers if a prepayment penalty is added to their loan terms.

Issue #14: Changing the uniform mortgage note to better reflect the growing use of prepayment penalties

The uniform mortgage note currently in common use in Maine contains the outright statement: "If you pay off early, you will not have to pay a penalty." In cases in which a prepayment penalty is part of the final terms, the closing package also includes a separate "rider" or amendment, contradicting the terms of the note and adding the prepayment penalty. The net effect of this approach is that a consumer who may be paying attention at the initial phases of the closing process (when the note that says "no prepayment penalty" is signed) may be paying less attention when the separate rider adding that penalty is also signed.

To address this situation, OCCR favors a change to the uniform note, such that it would include a "does/does not" option on its face with respect to the prepayment provision, similar to the current optional language found on the initial Truth-in-lending disclosure: "If you pay off your loan early, you ☐ may ☐ will not have to pay a penalty."

To that end, Section 7 of the proposed legislation, attached as Appendix #1, prohibits use of a rider to contradict and amend the specific provisions of a note that states that the loan is not subject to such a penalty.

Because this change would require re-drafting of a uniform document in general use at the present time, we feel that a delayed effective date for this proposal is appropriate.

Issue #15: Preventing "fee-padding"

In the Request for Public Comment, OCCR identified the development, or at least the perception of a development, that lenders were increasing fees and points to a level just below the threshold that would qualify a loan as a more heavily regulated high-rate, high-fee "Section 32" loan. We asked commenters to tell us whether this perception was a reality, and if so what could be done about it.

Our conclusion is that fee-padding is taking place in Maine, and as one way to address the practice we are recommending (*see* proposed bill attached as Appendix #1, Section 2) that the threshold of "points and fees" that triggers Section 32 treatment, be lowered from 8% of a loan amount, to 5%.

We base this proposal on the assumption that the supply of loans in this range (between 5% points and fees, and 8% points and fees) is, in economic terms, "elastic," such that establishing a new, lower level will not result in an unwillingness on the part of lenders to make the vast majority of those loans that currently fall in the range between 5% points-and-fees, and 8%. In other words, we believe that lenders making loans with points and fees totaling 6%, 7% or even 8%, will lower fees on many of those loans to 5%.

We also make this proposal with the knowledge that other nearby states (such as Massachusetts and Connecticut) already have established the lower 5% threshold in their state statutes. This change is also consistent with proposals advanced by Coastal Enterprises, Inc. (CEI), and by AARP in its model mortgage regulation act.

We feel that this proposal, in conjunction with stricter enforcement of the requirement that the GFE accurately disclose all fees within 3 days of application, should greatly reduce any "padding" of fees. (See more discussion of this proposal in Issue #16's comments, below, on whether loan broker compensation or mortgage finance charges should be "capped".)

Issue #16: Finance charge ceilings, and loan broker compensation caps

The August 30, 2006 Request for Public Comment asked whether Maine law should be amended to impose fee caps on broker compensation, or to establish maximum interest rates on mortgage loans. After review of the comments received, as well as looking to other states for model approaches, OCCR recommends against such maximum fee caps or rate ceilings. However, as stated in the discussion of Issue #15, above, we do recommend that the threshold for what constitutes a high-rate, high-fee loan under Maine law, be lowered from its current 8% of the loan amount in points and fees, to 5%.

This proposal to reduce the threshold level to 5%, which would bring Maine into line with nearby states such as Massachusetts and Connecticut, would not *prohibit* the making of a loan with a points-and-fees sum greater than 5% of the loan amount. Rather, it would merely subject such a loan to the additional consumer protections found in 9-A MRSA § 8-206-A, including: a) additional notices to consumers; b) limits on prepayment penalties; c) debt-to-income ratio tests before certain provisions can be included in the loan terms; d) limits on default rates of interest; e) a prohibition against negative amortization; and f) a prohibition against making loans solely on the value of the collateral.

Based on our experience in regulating the lending industry in Maine, we believe that lowering the threshold from an 8% points-and-fees trigger, to 5%, will not result in a substantial reduction in the loans available to Maine consumers. Rather, we believe that one of two things will happen. Either 1) loans will continue to be made in the 5% - 8% points-and-fees range, and those loans will be subject to the high-rate, high-fee protections; or 2) the points-and-fees sum will be lowered on many loans, such that they are made with terms at or below the new 5% points-and-fees threshold.

Issue #17: Regulating settlement agents

OCCR asked commenters whether or not independent settlement agents should be regulated, given the important role they play in the closing process. Although a majority of commenters favored the concept, the attached proposed bill (Appendix #1) does not contain such a provision. In the relatively short time utilized for this study, OCCR has not had an opportunity to determine 1) how many settlement agents practice their trade in Maine; 2) of the total, how many are already regulated professionally (for example, many such agents are attorneys or employees of law firms, answerable to the Bar Overseers for their closing-related activities); or 3) the cost to the State of establishing such a regulatory program, nor how that cost would be recovered.

If the Legislature believes that additional resources should be appropriated to address predatory lending issues, OCCR feels that initial consideration should be given to strengthening investigatory or legal resources at OCCR (*see* Issue #26, below), before considering implementing a program to regulate settlement agents.

As an aside, we note that the Legislature has already begun to recognize the importance of settlement agents, and of the need to bring some regulation to bear on that industry. 33 MRSA § 525, "Duty of Settlement Agent," is part of Maine's "Funded Settlement Act" enacted in 1999, c. 145, §1. This section requires settlement agents to promptly disburse funds and record mortgage documents after closing.

Issue # 18: "Net tangible benefit"

If there are two top hot-button issues in the national debate about predatory lending, they are 1) "net tangible benefits" and 2) liability of the secondary market. The latter issue is addressed in Issue #19, below, while we address the former in this section.

In the abstract, a net tangible benefit test seems simple to determine and easily enforced. Conceptually, such a provision prohibits the making of a loan unless, considering all aspects of the costs and terms of a loan, and considering all the financial circumstances of the borrower, the making of the loan would result in a net tangible benefit to the borrower.

However, this type of test would add a level of subjectivity to the lending process, and both lenders and loan brokers are united in strong opposition to such a measure. They feel that such a standard would give too much discretion to regulators, or to private attorneys in the instance of civil lawsuits or class actions, and that the determination of net tangible benefit could be dependent on information not always readily available to the lenders or brokers, such as the specific use to which the funds will be put, or to financial circumstances of the consumer that the consumer may not have revealed to the lender or loan broker during the application process.

Proponents can draw support from the fact that net tangible benefits tests were incorporated into one or more recent multi-state settlements (see the *Ameriquest* and *Household* global settlements), and that several states have also enacted net tangible benefit provisions. However, it is important to remember that the defendants in the multi-state settlements may have been amenable to such proposals because they were resolving thousands of complaints and paying millions of dollars in restitution and penalties, despite denying any wrongdoing. And a review of the state laws dealing with the provision reveals that in most instances its application is limited to refinances, often only those refinances closed a second time with the same lender.

Finally, it is important to remember that tools already exist to address patterns of unconscionable lending behavior. Lenders and loan brokers may retain their licenses only so long as they operate their businesses "fairly" (9-A M.R.S.A. §§ 2-302(2), 10-201). Further, the administrator may,

> *by regulation or order, . . . prohibit acts or practices in connection with:*
> *A. Mortgage loans that the administrator finds unfair [or] deceptive . . . ; and*
> *B. Refinancing of mortgage loans that the administrator finds are associated with abusive lending practices or that are otherwise not in the interest of the borrowing public.*
>
> 9-A MRSA § 8-206-A (16).

Such an approach, tailored to specific instances or trends discovered in this State, may prove both more flexible and more effective than statutory changes, which may have a detrimental effect on the secondary market valuations of Maine loans.

Issue #19: Secondary market accountability

With respect to certain proposals, this report concludes that the members of the lending industry can absorb changes imposed on it because in those areas there exists an amount of flexibility or elasticity of supply. However, in the areas of "net tangible benefit" (*see* Issue #18, above), and liability of the secondary market (discussed in this section), we feel that imposition of strict provisions could drastically and adversely affect the willingness of lenders and of the secondary market to make loans or to purchase them as investments, with the effect that less mortgage money would be available to Maine borrowers, or that the cost of borrowing those funds would greatly increase.

Since the secondary market (referred to as "assignees" in the Consumer Credit Code) is historically liable for rectifying errors made by the original lender *only* if the violations are "apparent on the face of the disclosure statement" (*see* 9-A MRSA § 8-209, "Liability of assignees"), that secondary market becomes reluctant to invest in loans if elements that are out of their control or knowledge (for example, the personal financial circumstances of the borrower) can be used to rescind a transaction or even to recover damages.

Therefore, increasing assignee liability is not among OCCR's recommendations contained in the attached draft legislation. We feel that the State's initial efforts at reform should be directed toward the front-line loan officers of loan brokers and lenders, and that secondary market liability issues should be addressed later if necessary, and only after receiving specific input and after reviewing the effect of assignee liability laws enacted in other states.

Issue #20: Increased regulation of servicers

Although OCCR identified servicing issues as a major cause of consumer complaints, we have not included specific servicing-related provisions in the draft legislation attached to this report.

In preparing this report, we reviewed the current legal obligations of servicers, including the requirement to provide toll-free consumer numbers (9-A MRSA § 9-304); to pay interest on escrow (§ 9-305); to pay taxes and insurance from escrow in a timely manner (§ 9-305-A); to respond promptly to requests for payoff figures (§ 9-305-B); and to provide a free accounting of all payments made in the past 15 months (§ 9-307(2)). Rather than impose additional requirements, OCCR will make every effort, with or without additional allotted resources, to more vigorously pursue any complaint-generated information regarding loan servicing, so as to impress upon servicers the importance of compliance in all such areas.

Issue #21: Effective notice of prepayment penalties

This issue is discussed with respect to Issues #13 and #14, above. Provisions relating to prepayment penalties have been incorporated into the draft legislation attached as Appendix #1; *see* Section 3 and Section 7 of that proposed legislation.

Issue #22: Requiring that "unpaid balance" figures reflect additional funds required as prepayment penalties

Because so many consumers have told OCCR that they didn't know they were subject to a prepayment penalty until they attempted to pay off their loan early, this proposal would have required that each time the lender notified the borrower of the unpaid balance on their loan (for example, upon request, or with each monthly statement, or at year-end), the lender would be required to add into that balance the prepayment penalty, to provide an accurate picture of the actual dollar amount necessary to pay off the loan.

We felt that the proposal was a simple and innovative way to prevent "payoff surprise." However, we have chosen not to include it in our proposed legislation. Like so many seemingly simple solutions to complex issues, this proposal would likely prove too difficult for lenders' billing computers to accommodate, at least just for borrowers in the State of Maine. We continue to feel that the concept has merit, and we also note the steps other states have taken to address, and indirectly discourage, such penalties (Massachusetts, for example, requires lenders to include prepayment penalties in the "points-and-fees" calculation to determine whether additional "Section 32"-type protections should be imposed). However, until or unless other states or federal regulators adopt the concept, we feel that it would be impracticable to require such calculations solely for Maine loans.

Issue #23: High attorney's fees in the initial states of pre-foreclosure or foreclosure

The Request for Public Comment raised the issue of high early legal fees, because in our experience assisting consumers who are delinquent in their payments it often seemed that lenders incurred significant legal fees immediately after files were sent to attorneys with instructions to initiate foreclosure. The imposition of such high fees hindered the abilities of all parties to "unwind" the situation and get the consumer back on track, because in addition to collecting all delinquent payments, interest and late fees, lenders also demanded reimbursement of legal fees incurred to date.

As much as we think this type of occurrence deserves scrutiny, we are now of the opinion that the situation should be addressed by 1) requiring the lenders to obtain specific information from their attorneys to demonstrate exactly how claimed fees were incurred in a short time; and, if necessary, 2) communicating with the attorneys and/or with the Bar Overseers in egregious or repeated cases. For this reason, the attached legislation does not contain measures to address legal fees incurred at the pre-foreclosure stage.

Issue #24: Private foreclosures

Although Maine is generally considered a "judicial foreclosure" state, Maine law still permits private foreclosures. However, the rules for such elements as service of process, and accounting for equity in the property foreclosed upon, differ between private and judicial foreclosures. We at OCCR feel that those types of provisions should be consistent in both public and private foreclosures, since the stakes (losing ownership of one's home) are the same. Therefore, the proposed legislation (Appendix #1, Section 12) proposes to apply the same type of service of process standards to private foreclosures as is now required in judicial foreclosures; and additional sections (Section 13 and Section 14) would repeal the current right of the foreclosing party to delay sale of property for 2 years and thereafter retain the entirety of the property with no duty to account to the consumer for any equity. Instead, we propose enactment of a requirement that the property be sold to the highest bidder, as is done in judicial foreclosures, with any equity in excess of the debt plus costs incurred in the action, being returned to the consumer after the sale.

Issue #25: Payoff requests

The issue of lenders' responses to payoff requests was included in our Request for Comment because we heard from consumers that when the consumers requested payoff figures, their lenders bombarded them with offers to entice them not to refinance with other lenders.

We have not included any new legislative proposal to address this issue. We now feel that any problems can be avoided 1) by vigorously enforcing current Maine law that requires a lender or servicer to promptly respond to a request for a payoff figure (*see* 9-A MRSA § 9-305-B); and 2) by likewise enforcing, where appropriate, the Consumer Credit Code's provision against unconscionable conduct by lenders (for example, 9-A MRSA § 9-402 prohibits the use of unconscionable conduct to induce a consumer to enter into a credit transaction). So long as lenders comply with the current statutory timeframes for producing a payoff figure, we are not of the opinion that they should be (or legally could be) prevented from offering their customers a better deal.

Issue #26: Possible addition of an OCCR staff attorney and/or an investigator to help prevent predatory lending practices

The proposal set forth in the Request for Public Comment to add an investigator and an attorney to OCCR's staff met with unanimous support from consumer groups and from industry commenters. We at OCCR feel that such a step would be extremely helpful in our efforts to protect consumers by quickly and flexibly respond to allegations by consumers, or by competitors, of predatory activity by lenders or loan brokers.

However, the attached bill does not propose specific authorization for those two positions. Given the current sentiment favoring the addition of state staff only as a last resort, we feel that the legislative committee that considers this bill (and the CEI anti-predatory lending bill as well) should make any such determinations after evaluating the need for such resources and after hearing from all parties on the subject.

Issue #27: Other related proposals

The attached bill (Appendix #1) contains three proposals not specifically addressed in the Request for Public Comment, but that are relevant to the issue of regulation of mortgage lending. The first is found in Section 1 of the bill. This section would permit (but not require) Maine to join in a major multi-state mortgage company licensing project that is currently underway in several states. What began as an effort to adopt uniform license application forms has now developed into a proposal, sponsored by two separate state regulatory associations (the Conference of State Bank Supervisors, or CSBS, and the American Association of Residential Mortgage Regulators, or AARMR), to operate a centralized licensing system that could accommodate the needs of lenders, especially large mortgage companies with operations in many states. Patterned after the national registration process that regulates the securities industry, this system is designed to reduce the burden on applicants and on participating states. Although many questions remain to be answered, OCCR thinks it prudent to put in place the legislation necessary to enable Maine to join this effort, if and when the time is right for such a move.

The second new issue is found in Section 4 of the bill, and it proposes to broaden coverage of Article 9 of the Consumer Credit Code to encompass a type of loan that few regulators knew existed until recently; namely, a second-lien purchase-money loan. Most commonly occurring when a lender splits up the total purchase amount into a first-lien loan and a higher-rate, second-lien loan, this type of loan is completely unregulated under current law due to the verbiage of 9-A MRSA § 9-101, “Scope,” which indicates that the Article covers only first-lien loans. OCCR is of the opinion that such loans deserve at least the protection granted first-lien purchase money or refinancing loans, if not the protections of the full Code applicable to second-mortgage, non-purchase, non-refinance loans.

The third and final “new” proposal is found in Section 8 of the bill attached as Appendix #1. It requires that loan brokers disclose to consumers amounts paid to those brokers by lenders in the form of yield spread premiums. Yield spread premiums increase as the interest rate on a loan increases, resulting in an incentive for a loan broker to arrange a high-cost loan even if the consumer may qualify for a lower rate. We do not propose to restrict the payment of such premiums; only to require that it be disclosed to the borrower. We feel this is an important step toward the goal of financial transparency in the consumer-broker relationship.

SUMMARY

We feel the above steps, as further modified or supplemented through the legislative process, will play an important role in helping to combat predatory mortgage lending in Maine. We are also aware that the so-called CEI bill will also be considered by the Legislature during its upcoming session, probably by the same committee, and at or about the same time. While the OCCR proposals are more moderate than those proposed by CEI, we feel that the OCCR provisions are well-suited to the specific issues that have arisen in this State, and also to Maine’s limited market share for mortgages and its concomitant limited ability to influence major national lending forces. However, we also feel strongly that CEI’s bill deserves serious debate, since Maine consumers will in the end benefit from a vigorous discussion of all viable approaches to the challenge of preventing predatory mortgage lending.

Dated: ____________________________________

William N. Lund, Director
Office of Consumer Credit Regulation

123rd MAINE LEGISLATURE

FIRST REGULAR SESSION - 2007

Legislative Document **No. ___**

An Act to Prevent Predatory Mortgage Lending Practices

Be it enacted by the People of the State of Maine to read:

Sec. 1. 9-A MRSA, Section 6-104-A is enacted to read:

Sec. 6-104-A. For purposes of participating in the establishment and implementation of a uniform multistate automated licensing system (hereinafter the "system") for loan brokers, supervised lenders that are not supervised financial institutions, and individual loan officers thereof, the director of the Office of Consumer Credit Regulation may:

A. Modify by rule the license renewal dates set forth in sections 2-302(1) and 10-201;

B. Establish by rule such new requirements as are necessary for the State to participate in the system, including authorizing the system to collect license fees on behalf of the state and remit those fees to the State, authorizing collection fees by the system to pay for its services, amending definitions in this Title to conform with uniform forms utilized by the system, authorizing the system to process and maintain license records, and authorizing use of the system's uniform forms, upon the director's finding that each new requirement is consistent with the public interest and the purposes of this Title; and

C. Require a credit and background investigation of each applicant for a license as a loan broker, a supervised lender that is not a supervised financial institution, or a loan officer thereof, by means including fingerprint checks for state and national criminal histories, commencing at such time as the State joins the system pursuant to this section. The cost of such investigations must be charged to the applicants. Information obtained or held by the director pursuant to this subsection shall be non-public pursuant to section 6-116 and not subject to disclosure.

Sec. 2. 9-A MRSA §8-103, subsection F-1 is amended to read:

F-1. "High-rate, high-fee mortgage" means a consumer credit transaction, involving real property located within this State, that is considered a "mortgage" under Section 152 of the federal Home Ownership and Equity Protection Act of 1994, 15 United States Code, Section 1602(aa) and subject to the regulations adopted pursuant thereto by the Federal Reserve Board, including 12 Code of Federal Regulations, Section 226.32 and the official staff commentary to the regulations as each may be amended from time to time except that for purposes of this title, the reference to “8 percent” in 15 United States Code, Section 1602 (aa)(1)(B)(i), and in corresponding regulations and official staff commentary, shall read “5 percent”.

Sec. 3. 9-A MRSA § 8-206, subsection 3 is amended to read:

3. In the case of a residential mortgage transaction, which is also subject to the Real Estate Settlement Procedures Act, United States Code, Title 12, Section 2601, et seq., good faith estimates of the disclosures required under subsection 1 shall be made in accordance with regulations of the administrator under section 8-201, subsection 3, before the credit is extended, or shall be delivered or placed in the mail not later than 3 business days after the creditor receives the consumer's written application, whichever is earlier. If the disclosure statement furnished within 3 days of the written application contains an annual percentage rate which is subsequently rendered inaccurate within the meaning of section 8-106, subsection 3, the creditor shall furnish another statement at the time of settlement or consummation. If the disclosure statement furnished within 3 days of the written application indicates that the consumer will not be assessed a prepayment penalty, and if that statement is subsequently rendered inaccurate, the creditor shall notify the consumer of that change as soon as practicable, and must also furnish a corrected statement at the time of settlement or consummation.

Sec. 4. 9-A MRSA § 9-101 is amended to read:

Article IX

Consumer Credit Transactions Made to Acquire Real Estate or Secured by First-Lien Mortgages

Part 1

General Provisions

§9-101. Scope

This article applies to all consumer credit transactions made by creditors that are not supervised financial organizations, that are made to finance or refinance the acquisition of real estate or the initial construction of a dwelling, or that are secured by a first-lien mortgage on real estate.

Sec. 5. 9-A MRSA §9-303-A is enacted to read:

§ 9-303-A. False information on application for credit

A supervised lender, or any loan officer thereof, may not knowingly permit, encourage or assist a consumer to submit false information on any application for credit, nor may a supervised lender or loan officer thereof knowingly falsify such information on a consumer's application.

Sec. 6. 9-A MRSA §9-303-B is enacted to read:

§9-303-B. Rate locks

If a supervised lender charges a consumer a fee to lock in a certain interest rate for a certain length of time, that supervised lender shall:

1. Take such steps as are necessary to actually secure or guarantee the specified rate for the appropriate length of time;

2. Select a time period within which the loan can reasonably be expected to close; and

3. Utilize good-faith efforts to close the loan within the rate lock period.

Sec. 7. 9-A MRSA § 9-303-C is enacted to read:

§ 9-303-C. Prepayment penalty riders

No supervised lender may impose a prepayment penalty provision through use of a rider or amendment to the loan contract if the terms of the loan contract state that no such prepayment penalty shall be imposed.

Sec. 8. 9-A MRSA §10-302 is amended to read:

§10-302 Requirement for written agreement

Each agreement between a consumer and a loan broker must be in writing, dated and signed by the consumer and must include the following:

1. A full and detailed description of the services to be performed for the consumer, including all guarantees and all promises of full or partial refund of fees paid, whether or not services are completed, and the length of time for which the agreement remains in effect before return of the fees for nonperformance can be required by the consumer;

2. The terms and conditions of payment, including the total of all payments to be made by the consumer ~~for the service~~ or by any other person or entity, whether to the loan broker or to some other person; and

3. The following notice:

> NOTICE TO CONSUMER: Do not sign this agreement before you read it. You are entitled to a copy of this agreement.

Sec. 9. 9-A MRSA §10-304-A is enacted to read:

§10-304-A. False information on application for credit

A loan broker, or any loan officer thereof, may not knowingly permit, encourage or assist a consumer to submit false information on any application for credit, nor may a loan broker or loan officer thereof knowingly falsify such information on a consumer's application.

Sec. 10. 9-A MRSA §10-304-B is enacted to read:

§10-304-B. Rate locks

If a loan broker collects a fee from a consumer to lock in a certain interest rate for a certain length of time, that loan broker shall:

1. Take such steps as are necessary to actually secure or guarantee the specified rate for the appropriate length of time;

2. Select a time period within which the loan can reasonably be expected to close; and

3. Utilize good-faith efforts to close the loan within the rate lock period.

Sec. 11. 10 MRSA, Section 1327-A is enacted to read:

§ 1327-A. Solicitation using prescreened trigger lead information from consumer report

No lender or loan broker shall utilize unfair or deceptive practices when using prescreened trigger lead information derived from a consumer report to solicit a consumer who has applied for a loan with another lender or loan broker. Without limitation, it shall be unfair or deceptive:

A. To fail to state in the initial phase of the solicitation that the solicitor is not affiliated with the lender or broker with which the consumer initially applied;

B. To fail in the initial solicitation to conform to state and federal law relating to prescreening solicitations using consumer reports, including the requirement to make a firm offer of credit to the consumer;

C. To knowingly or negligently utilize information regarding consumers who have opted out of prescreened offers of credit or who have placed their contact information on the federal "do not call" list; or

D. To solicit consumers with offers of certain rates, terms, and costs, with intent to subsequently raise the rates or change the terms to the consumers' detriment.

Sec. 12. 14 MRSA § 6203(2) is amended to read:

§6203. Foreclosure without possession

If, after breach of the condition, the mortgagee or any person claiming under him is not desirous of taking and holding possession of the premises, he may proceed for the purpose of foreclosure in either of the following modes.

1. Public notice. He may give public notice in a newspaper of general circulation in the county where the premises are situated, if any, or if not, in a newspaper of general circulation in an adjoining county, 3 weeks successively, of his claim by mortgage on such real estate, describing the premises intelligibly and naming the date of the mortgage and that the condition in it is broken, by reason whereof he claims a foreclosure; and cause a copy of such printed notice, and the name and date of the newspaper in which it was last published, to be recorded in each registry in which the mortgage deed is or by law ought to be recorded, within 30 days after such last publication. All foreclosures of real estate mortgages between September 3, 1965 and February 8, 1966 and otherwise valid, except that public notice was given in a newspaper published and printed in whole or in part in the county where the premises are located rather than in a newspaper having its principal place of business in the county where the premises are located, are validated. For the purpose of this section a newspaper shall be defined as one printed in the English language and entered as second-class postal matter in the United States mails.

2. Service of notice. He may cause an attested copy of such notice to be served on the mortgagor or mortgagors, or in case of any recorded transfer or transfers of the mortgaged property since the giving of the mortgage, on the record holder or holders of the title of the mortgaged property at the time of the service of said notice, if he lives in the State, by the sheriff of the county where the mortgagor or the record holder of the title resides, or his deputy, by delivering it to him in hand or leaving it at his ~~last and usual place of abode~~ dwelling house or usual place of abode with some person of suitable discretion then residing therein; and cause the original notice and the sheriff's return thereon to be recorded within 30 days after such service. In case different mortgagors or record holders reside in different counties, then service shall be made of such notice by any sheriff or his deputy upon the mortgagors or record holders residing in the same county as such sheriff or deputy. In all cases the certificate of the register of deeds is prima facie evidence of the fact of such entry, notice, publication of foreclosure and of the sheriff's return.

Sec. 13. 14 MRSA § 6204-B is repealed.

Sec. 14. 14 MRSA § 6204-C is enacted to read:

§6204-C. Public sale following expiration of period of redemption

Upon expiration of the period for redemption, if the mortgagor or the mortgagor's successors, heirs or assigns have not redeemed the mortgage, any remaining rights of the mortgagor to possession terminate, and the mortgagee shall cause notice of a public sale of the premises stating the time, place and terms of the sale to be published once in each of 3 successive weeks in a newspaper of general circulation in the county in which the premises are located, the first publication to be made not more than 90 days after the expiration of the period of redemption. The public sale must be held not less than 30 days nor more than 45 days after the first date of that publication and may be adjourned, for any time not exceeding 7 days and from time to time until a sale is made, by announcement to those present at each adjournment. The mortgagee, in its sole discretion, may allow the mortgagor to redeem or reinstate the loan after the expiration of the period of redemption but before the public sale. The mortgagee may convey the property to the mortgagor or execute a waiver of foreclosure, and all other rights of all other parties remain as if no foreclosure had been commenced. The mortgagee shall sell the premises to the highest bidder at the public sale and deliver a deed of that sale and the writ of possession, if a writ of possession was obtained during the foreclosure process, to the purchaser. The deed conveys the premises free and clear of all interests of the parties in interest joined in the action. The mortgagee or any other party in interest may bid at the public sale. If the mortgagee is the highest bidder at the public sale, there is no obligation to account for any surplus upon a subsequent sale by the mortgagee. Any rights of the mortgagee to a deficiency claim against the mortgagors are limited to the amount established as of the date of the public sale. The date of the public sale is the date on which bids are received to establish the sales price, no matter when the sale is completed by the delivery of the deed to the highest bidder.

In addition, the mortgagee shall cause notice of the public sale to be mailed by ordinary mail to all parties who appeared in the foreclosure action or to their attorneys of record. The notice must be mailed no less than 30 calendar days before the date of sale. Failure to provide notice of the public sale to any party who appeared does not affect the validity of the sale.

Sec. 15. Effective date. This Act takes effect on January 1, 2008.

SUMMARY

This bill protects consumers from predatory mortgage lending practices. Section 1 is intended to increase the accountability of lenders and loan brokers operating across state lines by permitting the Office of Consumer Credit Regulation to participate in a uniform automated nationwide mortgage licensing system, once that system is developed and implemented by the American Association of Residential Mortgage Regulators (AARMR) and the Conference of State Bank Supervisors (CSBS). Section 2 adds consumer protections to certain high-cost loans by reducing the threshold for so-called high-rate, high-fee loans from a points-and-fees trigger of 8% of the total loan amount, to 5%. Section 3 requires that a consumer be specifically notified if a prepayment penalty provision is added to the consumer's mortgage note just before closing. Section 4 applies consumer protections to so-called "piggy-back" loans, that are second-lien mortgages used in conjunction with first-lien loans to purchase real estate. Sections 5 and 9 prohibit lenders and loan brokers from facilitating submission of false credit application information by a consumer. Sections 6 and 10 regulate the sale and issuance of "rate locks" by lenders and loan brokers. Section 7 prohibits inclusion of contradictory information about prepayment penalties in a consumer's closing package. Section 8 requires disclosure to a consumer of any "yield spread premium" to be paid to a loan broker by a lender. Section 11 prevents unfair or deceptive practices with respect to "trigger leads" derived from consumers' credit reports. Section 12 amends the private, non-judicial foreclosure statute by applying the same "service of process" rules as those that govern judicial foreclosures. Section 13 repeals the current private sale provisions for non-judicial foreclosures, and Section 14 requires a public sale in private foreclosures, as is currently required in judicial foreclosures, to protect consumers who have equity in their properties in excess of their mortgage amounts. Section 15 provides for a January 1, 2008 effective date, to permit lenders and loan brokers to modify forms and procedures to ensure compliance with the bill's provisions.

123rd MAINE LEGISLATURE

FIRST REGULAR SESSION - 2007

Legislative Document **No. ___**

An Act to Incorporate Federal Real Estate Settlement Procedures Act into the Consumer Credit Code

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Be it enacted by the People of the State of Maine as follows:

Sec. 1. 9-A MRSA, § 3-315 is enacted to read:

§3-315. Real estate settlement procedures.

A creditor and its loan officers shall comply with the provisions of 12 USC §2601 *et seq.*, the federal Real Estate Settlement Procedures Act of 1974, and its implementing regulation, Regulation X, 24 C.F.R. §3500 *et seq.*

Sec. 2. 9-A MRSA § 10-307 is enacted to read:

§10-307. Real estate settlement procedures.

A loan broker and its loan officers shall comply with the provisions of 12 USC §2601 *et seq.*, the federal Real Estate Settlement Procedures Act of 1974, and its implementing regulation, Regulation X, 24 C.F.R. §3500 *et seq.*

Sec. 3. Effective date. This Act takes effect January 1, 2008.

SUMMARY

This bill incorporates the federal Real Estate Settlement Procedures Act of 1974 (RESPA) and its implementing regulation into state law, applying important consumer protections to mortgage customers of supervised lenders and loan brokers.

REQUEST FOR PUBLIC COMMENT

in preparation for the

Maine Office of Consumer Credit Regulation's

REPORT ON PREDATORY MORTGAGE LENDING

August 30, 2006

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1. Introduction

The State of Maine Office of Consumer Credit Regulation has been asked to study the issue of so-called "predatory" mortgage lending, to identify the incidence of such activity in Maine and to make legislative recommendations to address the problems that are found.

To help us accomplish that goal, we are requesting input, both verbally at an upcoming September 11, 2006 opportunity for public comment, and in writing, from all interested parties. The purpose of this document is to suggest parameters for that input, so as to enable our office to arrive at "bottom-line" recommendations in the most efficient manner.

For purposes of this study, our office defines predatory mortgage lending as high-rate or high-fee lending, in which the rates or fees are materially greater than would be warranted in a truly competitive environment. In addition, we consider other factors that make a mortgage loan "predatory", including lending advanced on the basis of the security rather than on the borrower's ability to repay; lending practices that take unfair advantage of a consumer's susceptibility because of certain characteristics of the borrower (*e.g.,* unsophisticated youth; easily-confused elderly; language barriers; credit-damaged consumers); and loans containing features such as prepayment penalties, mandatory arbitration clauses or other terms or conditions that can harm a consumer, that the consumer cannot reasonably avoid and that are not justified by corresponding benefits to the consumer.

However, in conducting this study, it is not our intent to propose changes just for the sake of change. Our years of regulating supervised lenders and mortgage brokers, and our knowledge of practices and regulatory measures in other states, have taught us that this is a controversial area, and that the best approach likely lies somewhere between the extreme limitations, regulation and enforcement favored by some consumer advocates, and the "any product to any borrower, any time" approach favored by certain *laissez-fair* proponents of an unrestrained, free-market approach.

We view the purposes of anti-predatory lending laws as 1) to prevent predatory lending; and 2) to assist consumers who have been subject to predatory lending practices.

To ensure that our approach remains grounded in reality here in the State of Maine, we have reviewed data and findings from three separate sources: 1) consumer complaints to our office; 2) the results of our compliance examinations of supervised lenders and mortgage brokers; and 3) our investigations into specific allegations of predatory-type lending and brokerage activities.

We have also reviewed the recent multi-state settlements in the cases of Beneficial/Household (2004) and Ameriquest (2006), as well as the steps taken by many other states to address predatory mortgage lending.

This document organizes possible action areas in a sequential manner, by following the mortgage lending process from its beginning (when a consumer responds to an advertisement or is solicited for a loan), through the middle phases (closing and servicing), to the conclusion (early payment, final satisfaction of the debt and discharge of the mortgage, or collection and foreclosure). At each stage, we identify issues and questions that have arisen in the context of our regulation of the supervised lending and mortgage brokerage industry in our state in recent years. And with respect to each issue, we pose questions as a way of soliciting specific input on a suggested approach to deal with the identified activity or problem.

Interested parties do not need to comment on each and every topic; rather, they are invited and requested to address those topics with which they are familiar and knowledgeable. In addition, commenters are not limited to the topics raised, since this is such a diverse area of inquiry and we do not wish to prevent discussion of other topics. However, our approach is designed to assist all parties by providing a framework within which to organize presentations and input.

2. The Sequential Steps in the Mortgage Loan Process

A mortgage loan may or may not be "predatory" from its inception. Rather, coercive or misleading elements can arise at various stages of the process. In other words, a loan product that is not necessarily predatory can be made predatory in the way that it is marketed or brokered. It can gain predatory aspects at closing, when it is sold to the secondary market, when it is serviced or when a consumer attempts to refinance the original debt. Because of this characteristic, an appropriate and holistic approach to combat predatory lending involves an evaluation of the entire process, to determine what measures should be taken to affect each stage of the lending process. Therefore, we have separated the process into its component parts.

The mortgage loan process takes place in several steps:

A. Advertising and solicitation (broker or lender). Consumers and brokers or lenders initially get together as a result of different forces and events. These actions include media advertisements, referrals, "trigger lead generating" services, Registries of Deeds searches and consumers' searches on the Internet. This initial process can "set the stage" for a predatory loan, since it provides an opportunity for the broker or supervised lender to evaluate the cognitive abilities, level of sophistication, and potential malleability of the consumer. In our experience, misleading sales tactics lead to undesirable loans, and so the focus here is to increase ethical standards and accountability of the brokers and lenders, and to increase the accuracy of the sales presentations.

B. Application. This stage involves the conveyance of financial documents and information from the consumer to the lender or broker. Within 3 days (if RESPA and Truth-in-Lending laws are complied with) it involves receipt by the consumer of an initial cost-of-credit disclosure and a "good faith estimate" (GFE). Money generally starts changing hands at this stage, through application fees and/or costs incurred for appraisals, credit reports, and other upfront expenses.

C. The gathering of information, including appraisals and credit reports. The period of time between the application and the closing is extremely important. Among other things, it is often the time when a "bait and switch" process will develop. In addition, if this "gathering of information" process takes longer than anticipated, the consumer's rate lock may expire, subjecting the consumer to higher interest costs. And finally, in those cases in which collusion or pressure between or among lenders and appraisers is alleged, this is the time period during which those relationships result in decisions that may be detrimental to the consumer.

D. Closing; payoff of prior liens, and payment to broker (if any) by consumer and/or by lender as Yield Spread Premium. The closing is the culmination of all previous activity. As the reader will learn from the results of consumer complaints to the OCCR (*see* part 3, below), many Maine residents report that the closing is when they are first made aware of expensive changes in the costs or terms of their pending loan. While the supervised lender, mortgage broker or settlement agent may feel very comfortable at a closing, the average consumer is often confused and intimidated. Asked to sign between 10 and 20 documents, far too numerous and too long to read in the time allotted, the consumer may rely for guidance on a settlement agent who in fact works for the supervised lender. Among the documents may be new, revised good faith estimates or cost disclosures, or mortgage notes that indicate that the loan is not subject to a prepayment penalty, only to be specifically overridden by a "Rider" farther down in the package that establishes such a penalty. The consumer may discover that some of their high interest costs will be rebated to the mortgage broker as a type of reward (a yield spread premium) for bringing a willing borrower to the supervised lender. A consumer who discovers higher costs or more onerous terms than expected is faced with a Hobson's choice: stop the process, or go through with it. And if the consumer has complaints against the closing agent, the consumer may quickly find out that settlement agents are not regulated under Maine law.

E. Assignment of loan to secondary market. The vast majority of loans are almost immediately packaged and sold on the secondary market. The net effect of this practice is to distance the original mortgage broker and supervised lender from the transaction, limiting almost completely a consumer's ability to resolve issues that arise at, or soon after, closing.

F. Servicing, including payment of taxes and insurance through use of escrowed funds. Once the loan makes its way to the secondary market, it is often split into various components or functions (the "servicing" is separated from the remainder of the investment), and servicing is subcontracted to specialists. Consumers with questions about the proper crediting of payments, about escrows for taxes and insurance, or about payoff figures or collection tactics, find themselves dealing with out-of-state (and out-of-country) servicers who are often busy handling millions of other accounts.

G. Pre-payment (if any). Consumers who are either enticed to refinance, or who are attempting to get out from under a high-cost loan that they now find to be more expensive than others available in the marketplace, often discover for the first time that their existing loan contains a prepayment penalty, usually for the first 3 years.

H. Collection and/or foreclosure (if any). Consumers who default on their mortgage find that their costs accumulate quickly. Attorney's fees are assessed to the borrowers under most mortgages, and several thousand dollars of those fees often accrue immediately when a file is referred to a foreclosure attorney, even if an action is not filed in court. And in Maine, lenders can still use an archaic method of "private" foreclosure, which does not involve the public filing of any documents in court.

I. Final payoff. Consumers attempting to obtain final payoff figures sometimes find such figures difficult to determine, and current lenders may use this delay as an opportunity to aggressively market the consumer to stay with the current lender.

3. Data from Complaints Against Licensed Supervised Lenders and Mortgage Brokers

Our office's computerized complaint tracking system maintains records of consumer complaints under general categories (*e.g.*, mortgages, debt collection, credit reporting). However, those records do not contain data in sufficient "subcategorized" detail to be helpful for a specialized study such as the present one. For that reason, the OCCR staff retrieved more than 125 original mortgage-related consumer complaints received between June 2005 and June 2006, and analyzed each file in order to derive the specific cause of the complaint. That analysis revealed the following results, organized in time sequence, starting with those relating to the marketing of the loans, and ending with payoff and discharge issues.

SPECIFIC TOPIC OF COMPLAINT	PERCENTAGE OF TOTAL
Telemarketing/trigger lead generation	8%
Loan application complaints	4%
Terms and costs increased at closing	20%
Servicing/incorrect crediting of payments	12 ½%
Escrow complaints	11%
Incorrect reporting to credit agencies	4%
Didn't know loan had pre-pay penalty	8%
Payoff/mortgage discharge complaint	9%
All other/miscellaneous	23 ½%

These findings are significant in a number of different ways. First, they serve to highlight the most common complaints (*e.g.*, 20% of consumers complained that when they arrived at their closings, they learned that the terms of their loans were less favorable than expected, or that their costs were greater than expected; and more than 12% of consumers write to us with servicing or payment-crediting complaints). However, even the smaller numbers above are important, because they represent Maine consumers who were so upset that they located the state agency responsible for supervision of licensed lenders and brokers, wrote to us, and followed through with their written complaints.

4. Questions Raised as a Result of OCCR Compliance Examinations

In addition to responding to consumer complaints, the Office of Consumer Credit Regulation also conducts compliance examinations of licensed lenders and loan brokers. The exam team reviews loan documents and responds to questions regarding whether or not certain loan products can be offered in Maine. In a typical year, the small exam team manages to review the records of more than 300 supervised lenders and creditors, and more than 30 mortgage brokers. Of all the OCCR's personnel, members of the exam team have the most direct day-to-day communications with lenders and brokers, and as such the exam team receives direct input on a daily basis from regulated entities.

An analysis of 248 mortgage company and broker exams conducted during the past 12 months reveals 109 instances of incomplete brokerage contracts; 58 incorrect or incomplete Truth-in-Lending disclosures, 24 instances in which no early or final T-i-L disclosure was provided, and 15 occasions in which the disclosure did not match the terms of the note. In addition, while most lenders examined indicated that they made Section 32 loans in other states, they had made no such loans in Maine during the past year.

Our exam team has raised the following questions, based on reviews of company records and on questions posed by regulated companies:

A. How many high-rate, high-fee loans are actually being made in Maine? Examiners pose this question because they report finding only a miniscule number of true "Section 32" (high-cost, high-fee) loans that qualify for disparate treatment under federal and Maine law. They find many loans that involve fees, costs and interest that fall just below the levels that trigger the additional protections. If it's true that not many Section 32 loans are being made, it means that the "target" loans of the upcoming study should be those loans that do not trigger the Section 32 treatment, but that nonetheless reveal predatory features.

B. If lenders are, as we suspect, staying just below the levels of costs and fees that would make loans high-cost, high-fee, are they increasing costs on a per-loan basis to fill the gap in each file as much as they can? In other words, are they "expanding" fees as much as possible without triggering the high-cost status?

C. In addition to proposing measures to combat predatory lending, this report is also an opportunity to review steps taken in the past to protect consumers, to evaluate whether those measures do, in fact, reduce the risk of inappropriate lending, or whether the need for those measures has been superseded by changes in the marketplace or increased sophistication or demand among certain borrowers. To that end, the exam team asked whether Rule 250, which establishes standards and limits for so-called "alternative" (variable-rate and balloon) mortgages, be eased to permit additional loan products to be offered, if those products have achieved acceptance on the secondary market and in other states?

5. Questions Raised as a Result of OCCR Investigations

When serious allegations are brought to the attention of the Office of Consumer Credit Regulation, or when the agency finds patterns of alleged violations by licensed companies, the Consumer Credit Code empowers the agency to conduct an investigation, including taking depositions, holding hearings and compelling evidence. Over the past several years, the agency has revoked the licenses of several loan brokers, and has received reliable, sometimes-troubling information alleging wrongdoing by mortgage brokers, collaboration between appraisers and loan officers, and questionable referral procedures among various segments of the real-estate and mortgage industry. In addition, our awareness has been increased regarding "yield spread premiums" and their resultant incentive for brokers to arrange very expensive loans for consumers so as to maximize that yield. And finally, we have learned that loan officers are not infrequently quietly fired from one company due to bad acts, but then quickly find employment with other companies.

Among the questions resulting from our investigations:

A. Have lenders/brokers formed alliances or relationships with appraisers that lead to inflated appraisals and the granting of risky, undersecured loans?

B. How does OCCR effectively keep "problem" loan officers out of the profession? How can our agency encourage or require employers to disclose when a loan officer has been fired for wrongdoing? Will the new loan officer registration program, and the upcoming loan officer education requirements, help to address this situation? [Note: The OCCR will treat this question of loan officer education separately, in the rulemaking process that will be initiated simultaneously with the drafting of the upcoming predatory lending report.]

C. Given that a loan broker is not required to act in the borrower's best interest, and in fact that the loan broker is sometimes rewarded financially for acting <u>against</u> the borrower's best interest, should a broker's self-interest be disclosed to the consumer?

6. Specific Areas of Inquiry, and Questions Posed to Interested Parties for Comment

A. Advertising and solicitation

1) *Mortgage "trigger leads"*

Discussion: Consumers and lenders have complained to OCCR concerning the use of "trigger leads." In this practice, a lender that subscribes to the service receives information that a consumer has recently applied for a mortgage loan, so that the subscribing lender can contact the consumer in an effort to solicit a loan. Specific complaints include:

1) that too much information is provided about the consumer (including credit scores, debt ratios, collections and inquiries);
2) the solicitations are misleading, in that the callers state or imply that they are affiliated with the lender with whom the consumer originally applied;
3) the solicitations do not include a firm offer of credit;
4) the names are not scrubbed against the "do not call" or "prescreening opt-out" lists; and
5) consumers who agree to change lenders, or brokers are "baited and switched" after they've committed to the second lender or broker.

The Maine Legislature has previously shown a willingness to enact laws to prevent this type of confusion; see 24-A MRSA § 2154, which prohibits an insurance company from using a bank's name without permission in solicitations to consumers.

Question #1 for public comment: Should the following amendment to the state's Fair Credit Reporting Act or the Maine Consumer Credit Code be enacted?

Title 10 MRSA sec. 1327-A is enacted to read as follows:

§ 1327-A. Solicitation using information from consumer report.

No lender or loan broker shall utilize unfair or deceptive practice when soliciting a consumer who has applied for a loan based, in whole or in part, on information in a consumer report. Without limitation, it shall be unfair or deceptive:

a) to fail to state in the initial phase of the solicitation that the solicitor is not affiliated with the lender or broker with which the consumer initially applied;

b) to fail in the initial solicitation to conform to state and federal law relating to prescreening solicitations using consumer reports, including the requirement to make a firm offer of credit to the consumer;

c) to knowingly or negligently utilize information regarding consumers who have opted out of prescreened offers of credit or who have placed their contact information on the federal "do not call" list; or

d) to solicit consumers with offers of certain rates, terms, and costs, and then to systematically raise the rates or change the terms to the consumers detriment.

2) Involvement of Broker vs. Lender

<u>Discussion</u>: Much to the surprise and dismay of consumers, the consumers often learn, after closing a loan that involves high fees or high rates, that the loan broker did not work to get the consumer the least expensive terms. In fact, in many instances the loan broker benefits by convincing the borrower to agree to a high-cost loan, since lenders makings such loans may reward brokers with generous fees or "yield spread premiums."

Question #2 for public comment: Maine law (9-A MRSA §§10-302 and 10-303) require that loan brokers provide consumers with a written contract and a written disclosure. Should these laws be amended to include a requirement that brokers disclose that they are not the agent of the consumer and may not be seeking the lowest-cost transaction? (See disclosure currently utilized by certain loan brokers, attached as *Exhibit 1*.) Are there other disclosures that are appropriate?

3) Supervised lenders vs. state-chartered banks and credit unions vs. federal banks or subsidiaries of federal banks.

<u>Discussion:</u> Mortgage loans in Maine can be made by mortgage companies (licensed supervised lenders), by state-chartered banks and credit unions, by federally-chartered financial institutions, or by non-bank subsidiaries of federally-chartered financial institutions. The identity of the lender makes a big difference in how the entity is regulated, and by whom. State regulators at the OCCR license and regulate non-bank

supervised lenders. These companies offer one major product – first-lien mortgage loans. The Maine Bureau of Financial Institutions oversees state-chartered banks and credit unions, which take deposits, make loans, meet strict capital standards and (for banks) meet CRA (Community Reinvestment Act) standards. Due to the actions and interpretations of federal bank regulators, the ability of states to enforce state laws against federally-chartered institutions and subsidiaries of those federally-chartered institutions has, to a great extent, been preempted. The preemptive assertions of federal regulators has no doubt been a significant factor in conversion of numerous state-licensed mortgage companies to subsidiaries of nationally-chartered banks and thrifts; see Exhibit #2 attached to the end of this document. Due to those assertions of preemption of state laws, federal regulators support the ability of federally-chartered institutions and their subsidiaries to offer products and features (such as variable-rate loans with prepayment penalties) that cannot be offered by licensed supervised lenders or by state-chartered banks or credit unions.

Question #3 for public comment: What percentage of so-called predatory lending is being conducted by lenders that claim to be exempt from state laws, and how does that percentage compare to the average market share of such lenders?

Question #4 for public comment: Given the efforts of federal regulators to preempt state law, how, if at all, can the State of Maine impose reasonable standards on federally-chartered financial institutions and their subsidiaries?

Question #5 for public comment: If the State of Maine adopts further provisions to protect consumers against the effects of predatory lending, should those provisions apply to state-chartered banks and credit unions that are already regulated by the Maine Bureau of Financial Institutions?

B. Available products

1) Should products continue to be restricted by Rule 250, even after they have met with general acceptance on the secondary market and in other states?

<u>Discussion</u>: OCCR's Rule 250 limits the availability of certain variable rate and balloon loan products. For example, as a general matter loans must be repaid within 31 years. However, lenders who benefit from the preemptive interpretations of federal regulators from Maine's laws are not similarly restricted, and many currently offer 40-year loans.

Question #6 for public comment: Should OCCR's Rule 250 be amended to remove certain restrictions if products offered by exempt lenders that do not contain those restrictions have found ready markets among Maine consumers without apparent detrimental effect? If so, how should the OCCR select the products or lenders to receive that exemption?

2) Effect of federal preemption -- brokers can arrange loans with terms that "violate" Maine law

Discussion: Brokers may "shop" a consumer's application to a variety of lenders, including national banks or bank subsidiaries that can (and do) ignore Maine state restrictions on, for example, prepayment penalties on adjustable-rate loans.

Question #7 for public comment: Should Maine's loan broker contract and disclosure laws (9-A MRSA §§ 10-302, 10-303) be amended to require a broker to disclose that some lenders with whom the broker may work to secure credit for the consumer, may be national banks or bank subsidiaries that are not required to comply with certain of Maine's consumer protection lending standards? (See conceptual broker disclosure, "Notice – Doing business with a federally-chartered lender or subsidiary", attached as *Exhibit 3*.)

C. Applying for a mortgage loan

Discussion: In the experiences of OCCR's exam, consumer complaint and investigative staffs, inflation of (or even creation of) income, assets and other elements of the application are common. We are aware of instances in which loan officers employed by loan brokers and supervised lenders have encouraged (or knowingly ignored) false statements, and even cases in which loan officers have falsified such information themselves without consumers' knowledge. While federal law is clear with respect to a *consumer's* potential liability for making false statements on an application, no such specific prohibition applies to *loan officers* who benefit from a closing a high-cost loan through receipt of generous points or commissions.

Question #8 for public comment: Should the following provision be added to Maine's Consumer Credit Code as applicable to loan brokers and supervised lenders?

> *A supervised lender or loan broker, or any loan officer thereof, may not knowingly permit, encourage or assist a consumer to submit false information on any application for credit, nor may a supervised lender, loan broker or loan officer*

thereof knowingly falsify such information on a consumer's application.

D. Gathering of information

1) *Issue of independence of appraisers*.

Discussion: Real estate appraisers are supposed to be guided entirely by strict ethical principles. However, supervised lenders or mortgage brokers can apply a great deal of economic pressure by selecting certain appraisers or by bypassing others. Nationally, this has been deemed such a problem that, for example, the recent *Ameriquest* settlement requires that appraisers be randomly selected from a pool of qualified appraisers. In Maine, while we have heard that certain supervised lenders and loan brokers have "go to" appraisers whom they can count on to establish a certain value for a property, specific proof is hard to find.

Question #9 for public comment: Is there a way to sustain the independence of appraisers while still respecting a supervised lender's or loan broker's freedom to utilize the free market? How can economic pressure or its effects be measured and combated?

2) *Rate lock time periods.*

Discussion: Rate locks have posed potential problems for Maine consumers for decades, especially in times of rising rates. The stated policy of the OCCR is that if a rate lock expires through the fault of the supervised lender or the mortgage broker, then the OCCR will hold the supervised lender or mortgage broker to the terms specified in the rate lock.

Question #10 for public comment: Should Maine law be amended to protect consumers by making clear that if a rate lock expires through the fault of a supervised lender or mortgage broker, then that lender or mortgage broker must make the consumer whole by obtaining a loan at the locked-in rate and terms?

E. Closing

1) RESPA -- should it be incorporated into Maine law?

Discussion: The Real Estate Settlement Procedures Act (RESPA) and the Good Faith Estimate (GFE). RESPA is a federal law that governs certain critical elements of the pre-closing relationship between and among the parties. For example, RESPA requires that consumers be given a good-faith estimate (GFE) that is designed to give the consumers a clear understanding of the terms of the upcoming loan transaction. In addition, RESPA governs under what conditions other parties to the transaction (*e.g.*, real estate brokers, lenders, loan brokers, appraisers, and referral services) can and cannot compensate each other with respect to the transaction. Despite the importance of this law, Maine law currently does not give Maine regulatory agencies the specific jurisdictional authority to enforce or interpret the law.

Question #11 for the public comment: Should Maine law be amended to incorporate all of (or selected portions of) RESPA, in order to bring authority, knowledge, expertise and enforcement to the state level? If so, how is this best accomplished?

2) What are the standards for providing a revised GFE if terms or conditions change?

Discussion: The single most frequent mortgage-related consumer complaint received by the OCCR (20% of our 2005-2006 sample) is that the terms of the loan change and/or the costs of the loan increase at the time of closing.

Question #12 for public comment: What can be done about the problem of "surprise" changes in terms or cost increases that are made known to the consumer at or close to the time of closing? If the lender has determined the terms of the loan substantially in advance of the closing, should the lender be obligated to disclose those terms to the consumer prior to closing?

3) The initial Truth-in-Lending (T-i-L) is the only place that pre-payment penalty is disclosed, and rules for redisclosure are unclear.

Discussion: OCCR has seen numerous occasions when one of the "surprise" revelations at closing is that a prepayment penalty has been added.

Question #13 for public comment: If a prepayment penalty is not disclosed as part of the early or initial T-i-L disclosure, should addition of such a prepayment penalty before or at closing require specific redisclosure?

Question #14 for pubic comment: Should the now-common practice of having a note that states "No prepayment penalty", but then having that provision be specifically contradicted by an addendum or rider later in the loan closing package, be prohibited or restricted? Put another way, should a consumer be "warned" that a clear-cut provision in a mortgage note can be superseded by a subsequent document in the large closing package? Should a closing agent by required to prove that such a provision was brought to the consumer's attention?

4) *Issue of "padding" of costs.*

Discussion: OCCR compliance examiners have reviewed closing packages in which it appears that fees and charges have been increased to a point just below the "Section 32" high-rate, high-fee levels. In fact, they have seen computer programs that appear designed to permit supervised lenders and loan brokers to calculate exactly how much can be charged without triggering the Section 32 coverage, with the result that such fees and costs are "adjusted" to the maximum possible amount.

Question #15 for public comment: Is there a way to establish appropriate levels or caps for specific fees and charges to avoid "padding"? Should such "padding" be viewed as an indicia of predatory lending? Would accurate fee disclosure on the Good Faith Estimate address this problem?

5) Should overall loan broker or supervised lender fees/points be limited?

Discussion: Neither federal nor Maine law currently contain any absolute limits on fees, costs or finance charges that can be assessed to consumers on first-lien mortgages. All that is required is that such charges be disclosed, with additional disclosures (and additional minor protections) being applied when loan costs surpass the levels triggering "Section 32" treatment.

Question #16 for public comment: Should Maine law be amended to establish maximum finance charges for supervised lenders, and/or maximum compensation for loan brokers?

*6) Role of settlement age*nt.

Discussion: Although consumers are able to hire an attorney to accompany them at a closing, most generally do not, relying instead on information conveyed by a settlement agent. As lending products have become more complex, and especially in instances in which costs, fees or terms have become less advantageous to the borrower between the time of the "good faith estimate" and the time of closing, the role of the settlement agent has become more and more important. However, under current law, settlement agents do not need to meet any standards, nor are they subject to any oversight or accountability. Many are non-attorneys, and many have affiliations or ties to other elements of the overall mortgage process (titles search, lending, title insurance, etc.).

Question #17 for public comment: Should Maine adopt any standards, or a system of accountability, for independent settlement agents?

7) *"Net tangible benefits."*

Discussion: Several states have adopted a relatively subjective standard for mortgage loans (other than purchase-money loans): To be permissible, the loan, looked at in its entirety, must constitute a "net tangible benefit" to the consumer. In other words, the consumer must be better off after receiving the loan, than they were before.

Question #18 for public comment: Should Maine adopt a "net tangible benefit" standard for refinance loans?

F. Assignment of loan to secondary market

Discussion: When a loan is sold on the secondary market, consumers may feel (often correctly) that they have lost any right to object to the way in which the application and loan process transpired. The Legislature took an important first step to increase accountability of portions of the secondary market several years ago when the Consumer Credit Code was amended to require registration of "loan servicers."

Question #19 for public comment: Is there a way to further increase the accountability of secondary market purchasers without interfering with the saleability of Maine loans? Should a secondary market purchaser be held responsible for errors made by the original licensed supervised lender?

G. Servicing, including payment of taxes and insurance through use of escrowed funds

Discussion: The "servicing/incorrect crediting of payments" category of consumer complaints constitutes 12 ½% of the total, while "escrow complaints" makes up another 11%. Combining the two under a general "servicing" category results in a 23 ½% figure, larger than any of the other given categories.

Question #20 for public comment: Recent changes to the Consumer Credit Code (9-A MRSA § 9-305-A) require timely payments from escrow. Is this provision sufficient, or should additional provisions be enacted to require accurate crediting of payments and prompt responses to disputes involving those payments (*e.g.*, RESPA provisions relating to escrow accounts)?

H. Pre-payment (if any)

Discussion: As set forth previously in this report, consumers often tell regulators that they are unaware of prepayment penalties until they arrange to refinance.

Question #21 for public comment: How can borrowers be more effectively notified that their loans contain prepayment penalties, especially if that feature is added late in the pre-closing process?

Question #22 for public comment: On periodic statements for loans with prepayment penalties, should Maine law require that the "unpaid balance" include the dollar amount of any prepayment penalty, since that penalty will have to be paid in order to pay off the loan in full?

I. Pre-foreclosure and/or foreclosure (if any)

1) *Accrual of attorney's fees pre-foreclosure.*

Discussion. In the experience of the consumer assistance staff at OCCR, when a case is sent to an attorney for foreclosure, attorney's fees of about $2,000 may immediately be added to the balance, even though no pleadings have yet been filed in court. This fact makes it very hard to "undo" the legal referral, even if the lender is willing to do so, since the dollar amount needed to "cure" the consumer's default increases by that legal fee.

Question #23 for public comment: Should foreclosure attorneys be restricted to adding to a defaulted balance only an amount representing work actually done and time actually spent on a case prior to the time pleadings are filed in court? What practices are permitted under the standard FNMA/FHLMC documents, and do Maine's attorneys conform to those practices?

2) *Non-public foreclosures still permitted in Maine.*

Discussion: Although most foreclosures are conducted in the public realm of the court system, private foreclosures are still permitted in Maine. In one case currently pending, service of process was allegedly made on a mentally-impaired granddaughter of the debtor (different service rules apply to private mortgages), and the paperwork was reportedly not passed on to the debtor. Because the entire subsequent foreclosure process took place in private and not in court, the debtor claims to have known nothing about the matter until the foreclosing party showed up to take possession. The private foreclosure law also permits the foreclosing party to retain the property for several years, and then sell it without the need to account to the former owner for any surplus.

Question #24 for public comment: Should private foreclosure be prohibited in consumer cases in Maine? If not, should the rules, such as the rules of service of process on and disposition of surplus, be amended to match those applicable to public (judicial) foreclosures?

J. Final payoff

Discussion: Consumers report to the OCCR that when they ask for a payoff, they are subject to hard-sales pitches to refinance with their current lender.

Question #25 for public comment: A recent amendment to the Consumer Credit Code (9-A MRSA § 9-305(B)) requires that supervised lenders, assignees or servicers provide a free payoff figure within 3 days of receipt of the request. Is the new law sufficient to protect consumers from being unduly pressured by their current lenders when they ask for a payoff figure, or are additional protections warranted?

K. Regulatory resources

Discussion: On a weekly basis, the OCCR receives evidence or tips from consumers or from legitimate supervised lenders or loan brokers, notifying the OCCR of alleged violations of Maine law. These can be as simple as alleging that a lender's advertising violates truth-in-lending regulations, or as complex as claims of unlicensed lending, fraud against consumers or the secondary market, or criminal activity. Our current examination team is responsible for all types of companies under our jurisdiction (*e.g.*, auto dealers, money transmitters, debt collectors, credit reporting agencies, and payroll processors), and routine examinations are scheduled weeks in advance for the benefit of small Maine companies. Therefore, members of the current exam team can be "pulled off" scheduled statewide exams only with great difficulty and inconvenience.

In addition, OCCR is the only agency within the department without an attorney on staff. Yet on a daily basis the agency fields extremely complex questions from supervised lenders and loan brokers involving the interplay between state and federal laws, the adequacy of certain disclosures, questions of permissible fees and other legal issues.

Question #26 for public comment: Should the OCCR request legislative authorization to hire an investigator and/or a staff attorney if such individuals could be added to the staff using existing resources and without raising annual fees or volume fees to supervised lenders or loan brokers?

L. Additional topics

Discussion**:** This request for public comment has focused primarily on addressing issues that have come to the attention of the OCCR through its regulation of loan brokers and supervised lenders. However, we may have missed some important areas or approaches, and we invite suggestions, especially suggestions patterned after successful approaches utilized by other states.

However, in our opinion, those suggestions will be most valuable if they:

1) address a problem that exists now, or will likely exist in the future, here in Maine;
2) recognize the limits of states' abilities to affect the lending practices of federally-chartered banks, and of the subsidiaries of those banks; and
3) recognize the importance of not taking steps that would result in a curtailing of mortgage funds to deserving Maine residents by disturbing the operations of the secondary market purchasing of Maine loans.

Question #27 for public comment: What additional steps could Maine take to address predatory mortgage lending practices, that would recognize the limited ability of the state to affect the activities of federal banks and their subsidiaries, and that would not interfere with the beneficial operation of the supervised lending and secondary market in making funds and a wide variety of loan products available to residents of this State?

7. Acknowledgment

The OCCR wishes to thank all who have offered to provide input, in writing or at the upcoming opportunity of public comment. If the report and recommendations resulting from this process have a positive impact on reduction or prevention of predatory mortgage lending, it will be because a wide range of knowledgeable and experienced individuals, companies and organizations contributed thoughtful input into the process. Thank you in advance.

August 30, 2006

Office of Consumer Credit Regulation
William Lund, Director

Exhibit 1 Additional disclosure form that some lenders are currently requiring mortgage brokers in Maine to use.

Mortgage Broker Fee Disclosure

You have applied to us – a mortgage broker – for residential mortgage loan. We will submit your application for a residential mortgage loan to a participating lender with which we, from time to time, contract upon such terms and conditions as you may request or a lender may require. The lenders have asked that this form be furnished to you to clarify the role of mortgage brokers. This form supplements other disclosures or agreements required by law that you should receive from us concerning your application.

SECTION 1. NATURE OF RELATIONSHIP. In connection with this mortgage loan:

- We may be acting as an independent contractor and not as your agent. If you are unsure of the nature of your relationship, please ask us for clarification.
- We have separate independent contractor agreements with various lenders.
- While we seek to assist you in meeting your financial needs, we do not distribute the products of all lenders or investors in the market and cannot guarantee the lowest price or best terms available in the market.

SECTION 2. THE BROKER'S COMPENSATION. The lenders whose loan products are distributed by us generally provide their loan products to us at a wholesale rate.

- The retail price we offer you – your interest rate, total points and fees - will include our compensation.
- In some cases, we may be paid all of our compensation by either you or the lender.
- Alternatively, we may be paid a portion of our compensation by both you and the lender. For example, in some cases, if you would rather pay a lower interest rate, you may pay higher up-front points and fees.
- Also, in some cases, if you would rather pay less up-front, you may wish to have some or all of our fees paid directly by the lender, which will result in a higher interest rate and higher monthly loan payments than you would otherwise be required to pay.
- We also may be paid by the lender based on (i) the value of the Mortgage Loan or related servicing rights in the market place or (ii) other services, goods or facilities performed or provided by us to the lender.

You may work with us to select the method in which we receive our compensation depending on your financial needs, subject to the lender's loan program requirements and credit underwriting guidelines.

The amount of fees and charges that you pay in connection with your loan will be estimated on your Good Faith Estimate. The final amounts will be disclosed on your HUD-1 or HUD-1A Settlement Statement.

By signing below, applicant(s) acknowledge receipt of a copy of this signed Agreement.

MORTGAGE LOAN ORIGINATOR APPLICANT(S)

____________________________ ____________________________________

[Date]

____

[Date]

Exhibit #2

Conversions of Supervised Lenders to National Bank Subsidiaries

(*unofficial tally*)

1. Alliance Mortgage Company, subsidiary of First Alliance Bank, non-renewal of Maine license by notice dated September 12, 2003

2. Avanta Mortgage, subsidiary of Avanta Bank

3. Banc of America Specialty Finance, Inc., surrendered Maine license January 9, 2002; subsidiary of Bank of America, NA

4. Banc One Mortgage Corp., returned Maine license December 9, 1999; will be making mortgage loans through national bank

5. Chase Manhattan Mortgage, surrendered Maine licenses November 2004; now subsidiary of national bank

6. CitiMortgage, Inc., returned 5 Maine licenses on September 10, 2001, based on Comptroller of Currency regulation; subsidiary of Citibank, NA

7. Corinthian Mortgage Corp., returned Maine license March 9, 2000 based on OTS opinion; subsidiary of South Bank, FSB

8. Deere Credit, Inc. and Farm Plan Corporation, surrendered registration December 2000; Accounts assigned to FPC Financial, FSB, a federal savings bank

9. Financial Freedom Senior Funding Corp., returned 2 Maine licenses February 20, 2001; subsidiary of Lehman Bros. Bank, FSB

10. First Franklin Financial Corp., surrendered license October 24, 2001; now branch of FFFC, Inc.

11. Fleet Mortgage Corp., surrendered license November 7, 2000; subsidiary of Fleet National Bank

12. Fleetwood Credit Corp., surrendered Maine license January 9, 2002; subsidiary of Bank of America, NA

13. FT Mortgage Company, subsidiary of First Tennessee National Bank; returned license February 19, 2001

14. Homeside Lending, Inc., returned 4 licenses February 20, 2002; purchased by Washington Mutual Bank, FSB

15. HSBC Mortgage Corporation, returned licenses September 2004; now subsidiary of national bank

16. Huntington Mortgage Co., surrendered license January 20, 1989; wholly-owned subsidiary of Huntington National Bank

17. Indy Mac, Inc., surrendered license July 1, 2000; holding company of Indy Mac Bank, FSB

18. Internet Mortgage, non-renewed by letter dated August 18, 1999; subsidiary of Horizon National Bank (OCC)

19. Ivy Mortgage, non-renew per letter of August 11, 2000; subsidiary of Staten Island Savings Bank (OTS)

20. LendEver Home Loans, returned licenses August 11, 2000; planning to merge with federal savings bank

21. Meritage Mortgage Corp., returned licenses October, 2004; now federal savings bank

22. New Century Mortgage Corp., transferred servicing to Ocwen, F.S.B., June 19, 2001

23. NexStar Financial Corp., surrendered license May 9, 2005; acquired by MBNA, NA

24. North American Mortgage Company, became a subsidiary of Dime Savings Bank; licenses returned August, 2000

25. PNC Mortgage Corp of America, surrendered licenses February 12, 2001

26. K Mortgage Corp. (S&B Mortgage Corp.), became part of Liberty Federal Savings Bank, September 24, 1999

27. Temple-Inland Mortgage Corp., surrendered licenses March 21, 2001; became operating subsidiary of federal savings bank

28. United Pan Am Mortgage Corp., surrendered license; will be division of federal savings bank, April 5, 1999

29. Wells Fargo, surrendered 14 licenses October 24, 2001 subsidiary of national bank (only remaining licensee: "Wells Fargo Financial Maine, Inc.")

30. WFS Financial, Inc., surrendered 7 licenses March 21, 2006; now wholly-owned subsidiary of Wachovia Bank, NA

Notice - Doing business with federally-chartered lenders

We are arranging a loan for you from a lender that is a federally-chartered lender, or an affiliate of a federally-chartered institution.

The lender may claim that the State of Maine's ability to enforce its laws against the lender are preempted by federal law and regulation. Therefore, the loan we are arranging for you may contain terms (such as a pre-payment penalty on a variable-rate loan) that would not be permitted if your loan were made by a lender regulated by the State of Maine.

In addition, if you file a consumer complaint about your loan with state regulators, those state regulators may be required to forward your complaint to federal regulators for resolution.

Date: ________________________ ________________________________

Consumer's Name