CFPB Update on Origination Rules

Presented by the CFPB and MBA
October 17, 2013

Transcript prepared by BuckleySandler LLP[1]

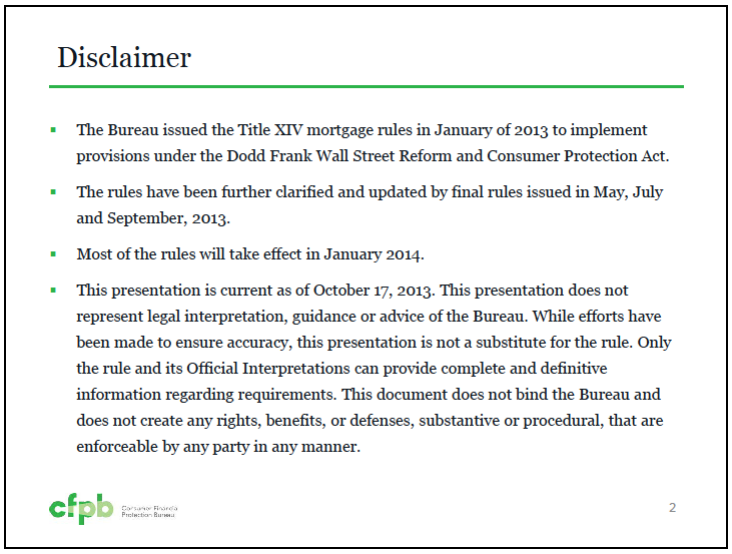
DAVE STEVENS: Good Afternoon everybody, this is Dave Stevens. I'm the President and CEO of the Mortgage Bankers Association. I want to thank you all for joining the call today. And as an, as an opening, obviously for many of you, this is the second of the series. We held a call yesterday and today is the follow up to focus on the new origination rules from the Consumer Financial Protection Bureau. Just as an outset, I think this is a great opportunity as we are thinking about this massive amount of operational readiness that we're working towards starting January, to be able to have these kinds of opportunities to at least hear feedback on some of the questions many of you have been asking about the various rules and I really want to applaud the Consumer Financial Protection Bureau, clearly the regulator at the epicenter of policy development for many of you for the effort they've put into to have an open and ongoing dialogue with the industry and the staff's willingness to participate in a webinar like this, as well as all of our MBA conferences where they have been active and engaged going through the various complexities around readiness for January. You will have a chance to… Live Q and A will not be available at the session today. I want to make that clear, but you can make inquiries that will be on the final slide of the presentation today and the information about how to make inquiries direct to the CFPB but again they will be covering as many of the commonly asked

[1] **The audio recording and original slides are available at: http://mortgagebankers.org/Compliance/cfpbrecordings.htm. The transcript is provided for informational purposes only and does not constitute legal opinions, interpretations, or advice by BuckleySandler. The transcript was prepared from the audio recording provided by the MBA and may have minor inaccuracies due to sound quality. In addition, the transcript has not been reviewed by the CFPB for accuracy or completeness. This transcript inserts an image of the slide that corresponds to the discussion, but all insertions are approximate because the audio recording does not consistently identify which slide is being discussed. This transcript also revises citations for consistency with the Code of Federal Regulations (*e.g.*, "1026.32(b)(1)(iii)" instead of "1026.32(b)(1)(3)").**

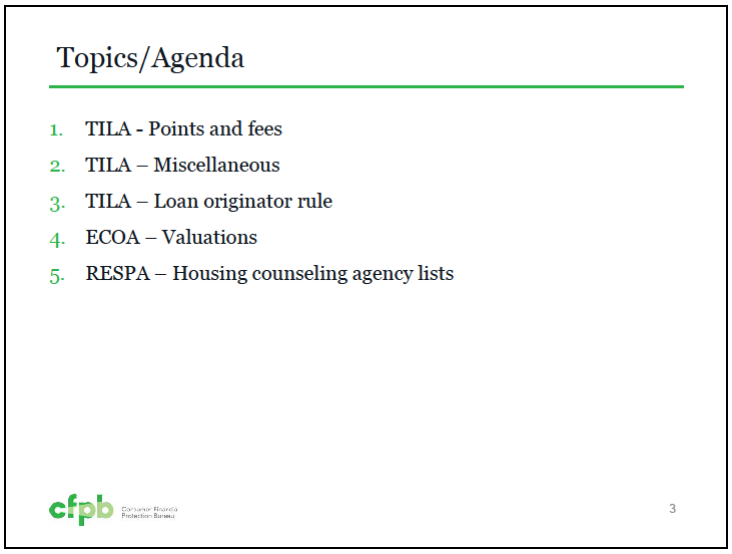
questions that they can get to during the session today. Joining us to start this off is Lisa Applegate from the CFPB. Lisa is the Mortgage Implementation Lead at CFPB. She joined the Bureau at the beginning of this year, after almost two decades at Fannie Mae to lead industry based support activities to aid in the implementation around the Dodd Frank Act Rules which were issued by the Bureau in January. Lisa was attracted to the Bureau role as an opportunity to bring her related GSE industry implementation leadership experiences to bear to make high impact contributions at a time, at an important time as the industry focuses on implementing the new rules and Lisa, thank you so much for joining us today.

LISA APPLEGATE: Thank you, Dave! And thanks to the MBA for inviting the Bureau to be here today to provide some updates to frequently asked questions on our origination rules, as well as yesterday, where we did so on the servicing rules. So we're very happy to be here, continuing the regulatory implementation support focus that we began earlier this year. One of our key priorities has been to bring increased clarity, certainty, and burden relief wherever possible and appropriate to address critical questions that we've heard from industry. To this end, we value the ongoing dialogue with all of the trade associations, including the MBA, as well as other industry stakeholders throughout the year as we surfaced and prioritized these questions. Today, members of the Bureau's Office of Regulations will provide unofficial, oral staff guidance, addressing certain frequently asked questions that we've heard persistently from industry about the Title XIV mortgage service, mortgage origination rules today. We hope this session is helpful as you're finalizing your implementations and preparing for the effective date of the rules. During this session, I will walk through the series of FAQs, across the rules, and three subject matter expert attorneys from the Bureau's Office of Regulations, Andy Arculin, Dan Brown, and Nick Hluchyj, will provide unofficial, oral guidance remarks.

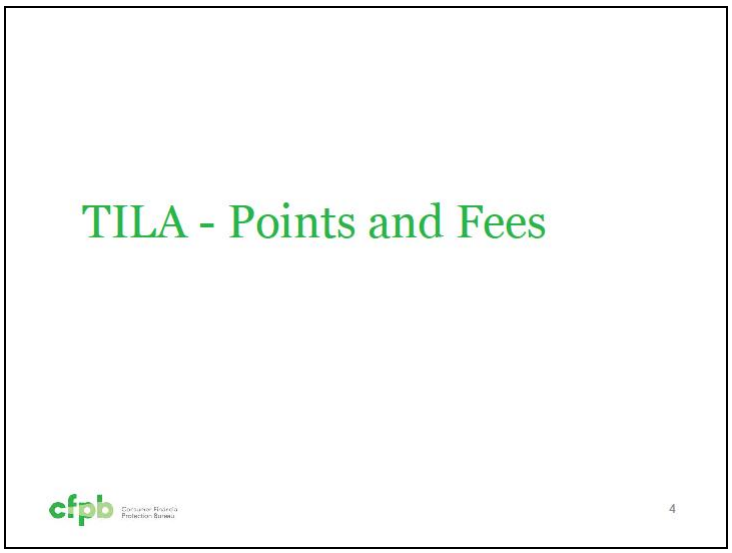
Before we start, let me draw your attention to slide two.



Although considerable efforts have been made to ensure accuracy of all remarks provided here today, this unofficial, oral staff guidance is not a substitute for the rules. Now let's get started.

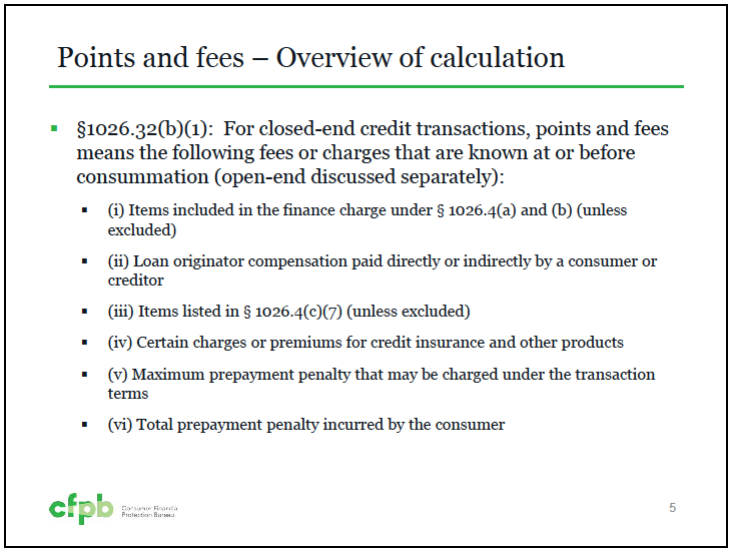


LISA APPLEGATE: **We've received many, many questions over the course of the year about points and fee calculations. Andy, can you walk us through the points and fees calculations, and, as you do, we can take up questions in context**?

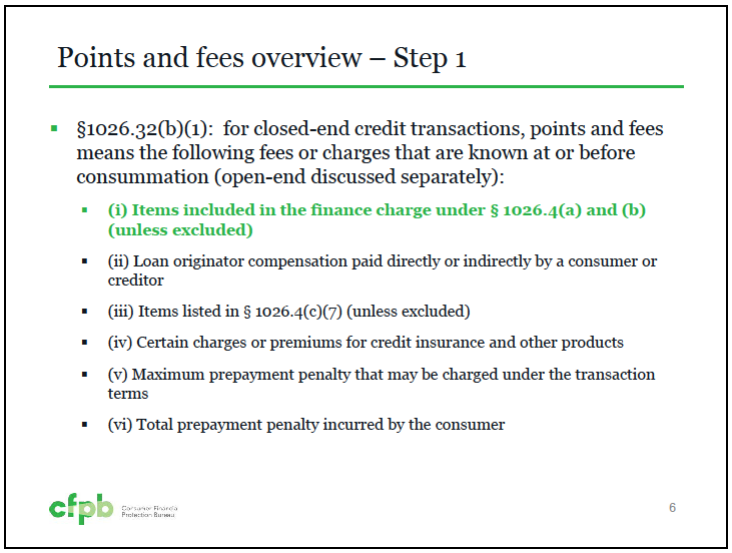


ANDY ARCULIN: Sure, so just a few things up front, I mean obviously, everybody knows that the points and fees calculation is relevant to two of our [inaudible – may be "rules"]. There's the ATR/QM points and fees cap, which applies to closed-end credit transactions, and then there's the HOEPA coverage test as well, which applies to both closed-end credit transactions and open-end credit plans. So, what I'm going to do, and we've gotten a lot of different questions, which Lisa will sort of cover as we go on, some just sort of asking for a walk through of the test, some asking about the treatment of specific charges under different prongs of the test, and then some really nitty gritty interpretive questions about the rules themselves. I'm going to try and focus most of my time on the third, but still thought it was useful just to sort of walk through the whole

test. You know, in general, if you look at, if you look at the whole points and fees test, the whole, you know, I appreciate that it can be maybe a little bit intimidating. But I think if you break it down into a step-by-step walk through, it's a lot easier to follow and a lot of the questions that keep coming up can be answered and I think are answered by the rules themselves.



So, we can, basically what we have here is just a very, this is an overview of the whole test. You know, its shorthand. You would want to go and actually look at the provisions, but basically we have, for closed-end credit transactions, and, you know, to put it up front 32(b)(2) is where you'll find a similar test for open-end credit. I'm going to talk about that at the end. Essentially, the first six prongs are the same, with some differences that relate to HELOCs as opposed to closed-end credit, then there's two additional provisions. For the most part, it's very similar, almost identical. And because ATR/QM applies to closed-end credit only, I'm going to start with closed end-credit and do a walk through and then just cover open-end at the end.

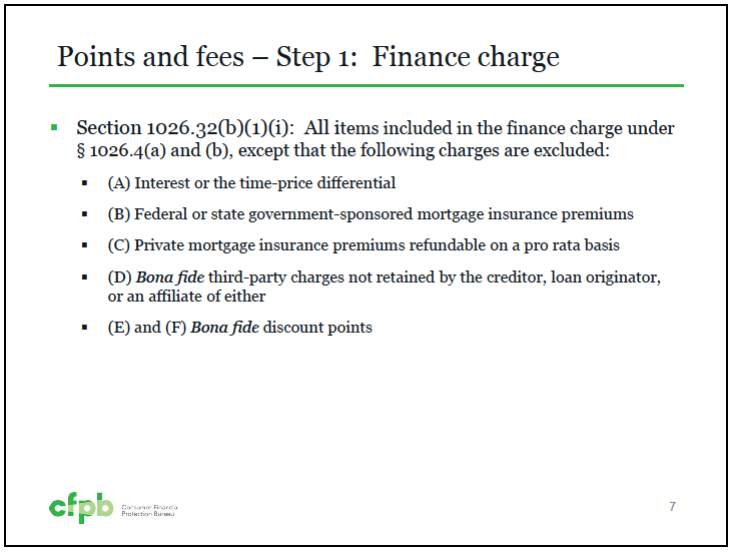


So, for closed-end credit, here's the test. It says, "For closed-end credit transactions, points and fees mean the following fees or charges that are known at or before consummation. The first is items included in the finance charge under § 1026.4(a) and (b) unless excluded." The finance charge is something that the industry should be familiar with. It is not something new. This brings in (a) and (b) charges into the points and fees calculation.

Once you've done that step, you move on to loan originator compensation, paid directly or indirectly by a consumer or creditor.

Then, you move on to items listed in § 1026.4(c)(7). These are "Real Estate Related Charges." We'll walk through these thoroughly in a minute. Then, you move on to certain charges or premiums for credit insurance and other products that are paid at consummation. A maximum prepayment penalty that may be charged and then total prepayment penalties incurred.

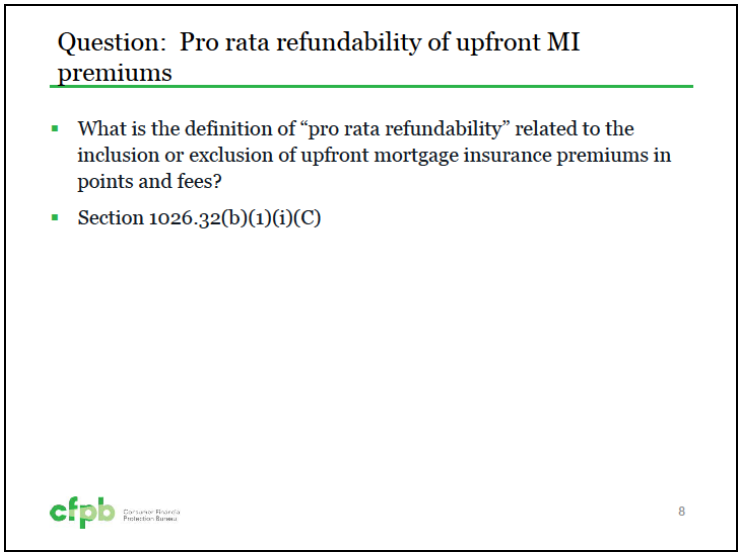
So that's the test as a whole, and you know, if you look at that, you know, it may look like a lot, but what I want to do now is just do a step-by-step, and for each step we'll dive into the specific interpretive questions that I know you're interested in hearing about. So let's go to the next slide.



Okay. Okay, so this is the, the first step is what I call the finance charge prong. This is § 1026.32(b)(1)(i). This says, "All items included in the finance charge under § 1026.4(a) and (b) except the following charges are excluded." I would also note that the end of (b) says that, you know, charges that are excluded under (c) through (e) are also excluded. That's in the regulation itself. There's a number of specific exclusions that are set forth here, that would otherwise be included in the finance charge. The first is interest or the time-price differential. And that's something we've heard a lot of questions about. Same with the second, which are federal or state government sponsored mortgage insurance premiums paid up front. The third, private mortgage insurance premiums, upfront private insurance mortgage premiums refundable on a pro-rata basis is something we will cover. And then *bona fide* third party charges not retained by the

creditor, loan originator, or an affiliate. Again, that's something we've heard a lot about, *bona fide* discount points for the last two prongs is something we've heard about.

A few things to note about this slide is that obviously (A) and (B) are just, you know, exclusions but (C), (D), (E), and (F) have specific conditions that apply to them, and for (D) it's *bona fide* third party charges not retained by the creditor, loan originator, or an affiliate of either and they're not required to be included in points and fees under other paragraphs in points and fees test such as (b)(1)(i)(c) and (b)(1)(iii) or (b)(1)(iv). So we can move on.

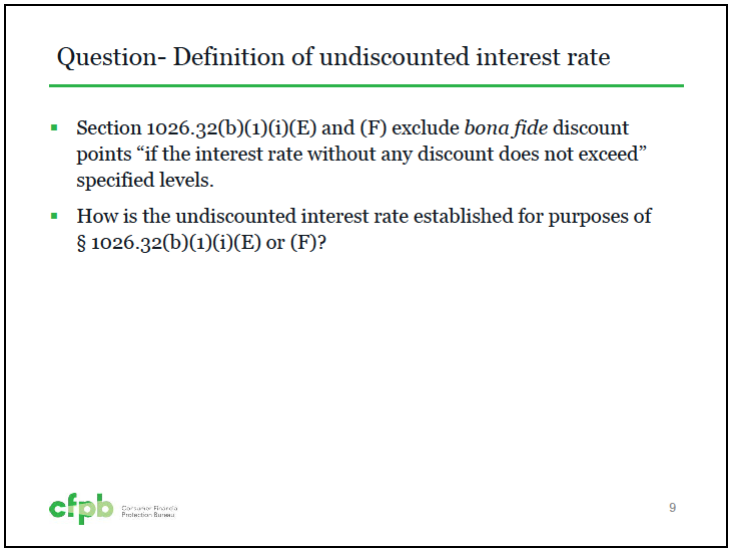


LISA APPLEGATE: Okay, so Andy, the first question related to this part of the test, relates to the pro rata refundability of upfront MI premiums. (b)(1)(i)(C) allows exclusion of monthly and annual PMI premiums. However, upfront premiums are only excludable if the premium is refundable on a pro rata basis, among other conditions. What is the definition of "pro rata refundability" related to the inclusion or exclusion of upfront mortgage insurance premiums in the points and fees?

ANDY ARCULIN: Okay, so the way that the Bureau interprets the term "pro rata refundability," first of all, I would just put out there that pro rata is not something that we've specifically defined in the rules. But there is a provision of Reg. Z, § 1026.2(b)(3) that says "Terms are given the meaning that they have under state law or contract, to the extent that they are defined under state law or contract." So, you know, one thing just to caution people about is that if this charge is given a specific definition under state law or under contract, you would want to look at that for the definition of pro rata. But as far as, just a, you know, assuming that's not the case, that's not a defined term under your applicable law, the Bureau interprets the term "pro rata" to basically mean proportionate, which is just the common definition given to pro rata. So, you know, this generally means that the refunds should be proportional to the amount of time remaining on the policy after [inaudible] paid off and the total term of the policy. So if you wanted to do it mathematically, you would say, refund equals total premium times time remaining over term of policy. So if you had a $3,000 premium and, you know, the premium

basically lasts for ten years, which is the point where the, the LTVs or loan to value ratio would go to 78% but you pay it off in year one. You would do 3,000 times 9 over 10, because its nine years remaining in your ten year term.

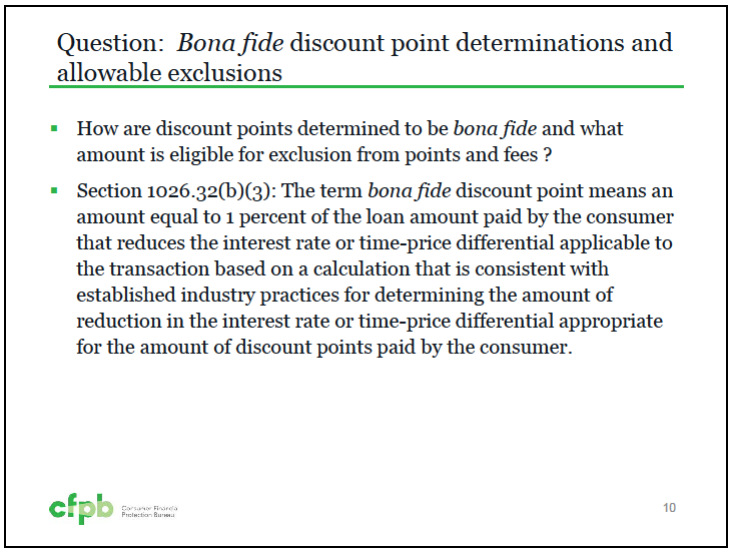
A few things to note, if a mortgage insurance policy is… basically, take the same mortgage insurance policy that's in effect for ten years, the upfront payment is for ten years but the premium is only refundable until say the loan to value reaches 85%, which would be in year eight, then the Bureau would not consider that, that refund to be pro rata within the meaning of the regulation. But again, you know, this is something where you would have to look and make sure that there's not a specified definition under state law or in the mortgage contract.



LISA APPLEGATE: Okay, great! Thanks very much, Andy. Let's move on to the definition of "undiscounted interest rate." Section 1026.32(b)(1)(i)(E) and (F) exclude *bona fide* discount points "if the interest rate without any discount does not exceed specified levels." How is the undiscounted interest rate established for the purposes of these provisions?

ANDY ARCULIN: Okay, So this, the term "undiscounted interest rate" is really, you know, in our view, a consumer specific exercise determining what that rate's going to be, you know? It's really, in layman's terms, it's the interest rate that, that consumer would get with no discount points, but what it means is, you know, it could be a little more technical and a little more precise than that, it's a zero point rate that may be calculated, but that… sorry. It's a rate that could be calculated and is available to the actual consumer. Something that would not be a *bona fide* discount point would be a zero point rate that could be calculated but is not available to that consumer. So, if, for example, if there's, if there's a no point rate that would be available to someone with a perfect credit score, but this borrower would not get that rate, because the borrower doesn't have a perfect credit score, that would not be the undiscounted interest rate. And then, in addition, the undiscounted interest rate also has to reflect line level price

adjustments and other adjustments used to compensate for additional risk and other factors of that particular consumer and the particular transaction.



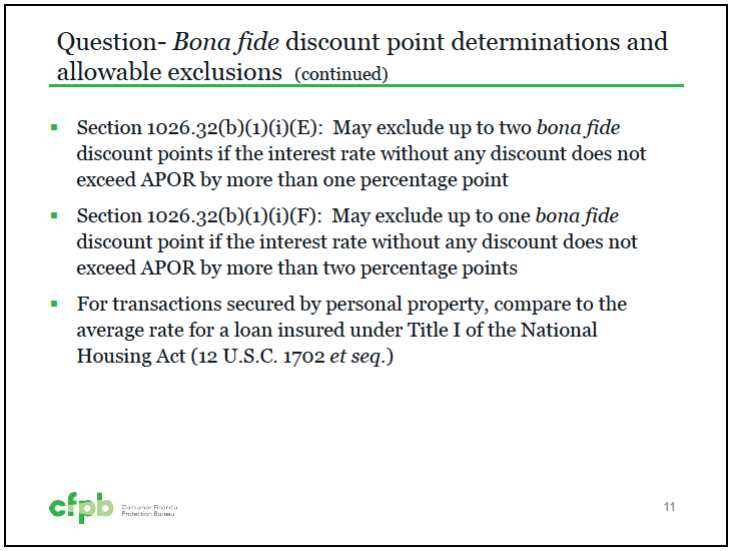
LISA APPLEGATE: Okay. Thanks very much. Let's stay on this topic, and talk about *bona fide* discount point determination and allowable exclusions. How are discount points determined to be *bona fide* and what amount is eligible for exclusion for points and fees?

ANDY ARCULIN: Okay, so there's really two questions here. One is what does *bona fide* mean? And one is what is excludable? What you have up on the screen is the reg text itself that defines the term "*bona fide*." It says, "The term *bona fide* discount point means an amount equal to one percent of the loan amount paid by the consumer that reduces the interest rate or time-price differential available to, applicable to the transaction based on a calculation that is consistent with established industry practices for determining the amount of reduction in the interest rate or time-price differential appropriate for the amount of discount points paid by the consumer."

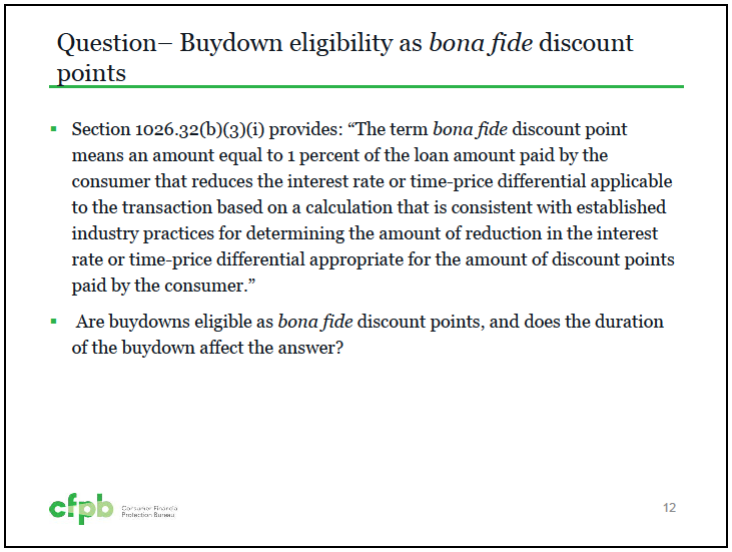
That's a lot of legalese, I understand. It essentially means "*bona fide*". . . sorry, we were having some sound issues but hopefully everyone can hear me better. I was going over just the definition of *bona fide* discount points. It's on your screen. And basically saying, what this means, if you really want to reduce it to layman's terms is, it's a discount point where you're actually buying down the interest rate and what you're getting in return for your money is in accordance with established industry practices. That's, that's really just kind of fundamentally what it means. And, you know, the rest is really, it's already set forth in the text but, that basically if you're, if you're, starting at the undiscounted interest rate, you're making a payment and, in accordance with industry practices, that payments reducing, the payments reducing your rate that it's a *bona fide* discount point.

The second question is, you know, what is actually excludable. The amount eligible for exclusion from points and fees, as a *bona fide* discount point, is limited to the amount, but for the payment of which the consumer would have paid the undiscounted interest rate.

So the amount excluded can't be greater than the amount actually paid by the consumer. You know, for example, the creditor can't take in some sort of secondary benefit that the consumers getting from a lower interest rate and consider that part of, part of, the amount that's excluded. It really has to be the amount of money that the consumer has paid.

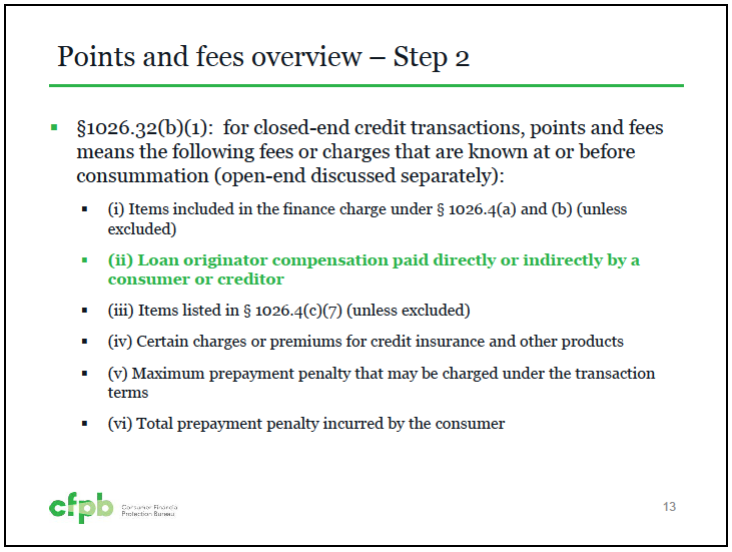


And then, what we have on the screen here are just some additional, these are some additional limitations on the amount of discount points that can be excluded based on the relationship of the undiscounted rate to the APOR – the average prime offer rate. So you can exclude up to two *bona fide* discount points if that interest rate, which doesn't exceed the APOR by more than one percentage point. But you can only exclude up to one, to be excluded by APOR by more than two percentage points. And the last bullet point is just a reminder that if you're dealing with transactions secured by personal property where there may not be an APOR available, then you compare the average rate for a loan insured under Title I of the National Housing Act.



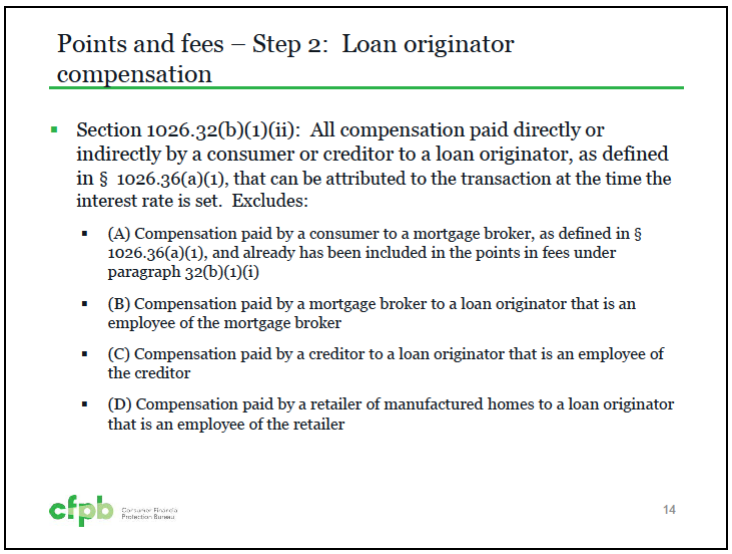
LISA APPLEGATE: Okay, great. Thanks very much. Before we leave the topic of *bona fide* discount points, let's do one last question. It's about buydown eligibility as *bona fide* discount points. Are buydowns eligible as *bona fide* discount points? And, does the duration of the buydown affect the answer?

ANDY ARCULIN: Yes, buydowns are eligible as *bona fide* discount points, as long as they're consistent with established industry practice and they meet the other qualifications of a *bona fide* discount point. Essentially, what this means is that there's no requirement under the rules that a *bona fide* discount has to apply for the life of the loan. It can be for a shorter time period, as long as it's a real *bona fide* discount point and what's being paid for is commensurate and is within established industry practices.



LISA APPLEGATE: Okay, great. Thanks very much. Okay, let's go on to step two of the points and fees overview.

ANDY ARCULIN: So, the finance charge was an area where we've gotten a lot of specific questions, so we spent a good bit of time on that. I won't spend a whole lot of time on the second prong, but just to cull it out, just sort of let you know what's happened here since the ATR/QM rule was finalized back in January. This is the provision, now you've presumably gone through the finance charge exercise. You've got your step one down, you've got all of your charges included. The next step is to look at 32(b)(1)(ii) for loan originator compensation that needs to be included. But the general definition is all compensation paid directly or indirectly by a consumer or creditor, to a loan originator, as defined in § 1026.36(a)(1). That's just the definition of "loan originator" under the loan originator compensation rule which can be attributed to the transaction at the time the interest rate is set.

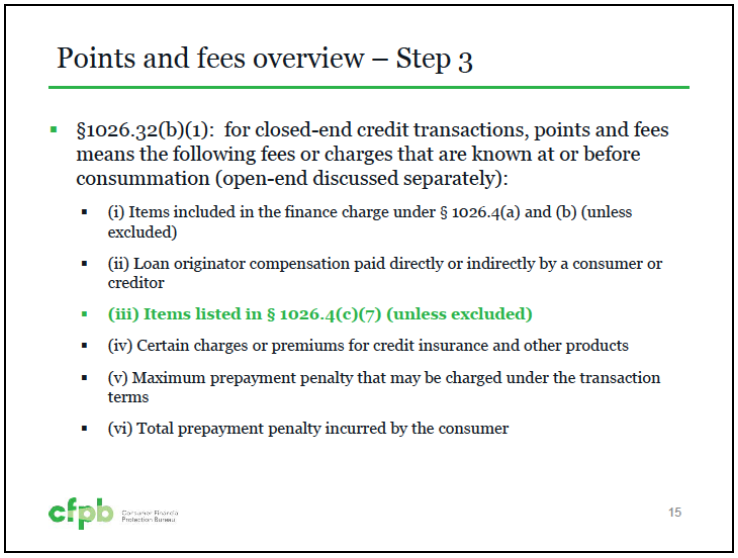


So, I think generally that the basic test is understood as far as I know at least. I know that, originally there was, at the time the ATR/QM rule was put out in January, you know, we were still working through what types of loan originator compensation would need to be included under this prong of the points and fees test and there's been two amendments to this rule [inaudible] since the rules have been finalized. So now we've excluded certain types of compensation from the test that you should be aware of.

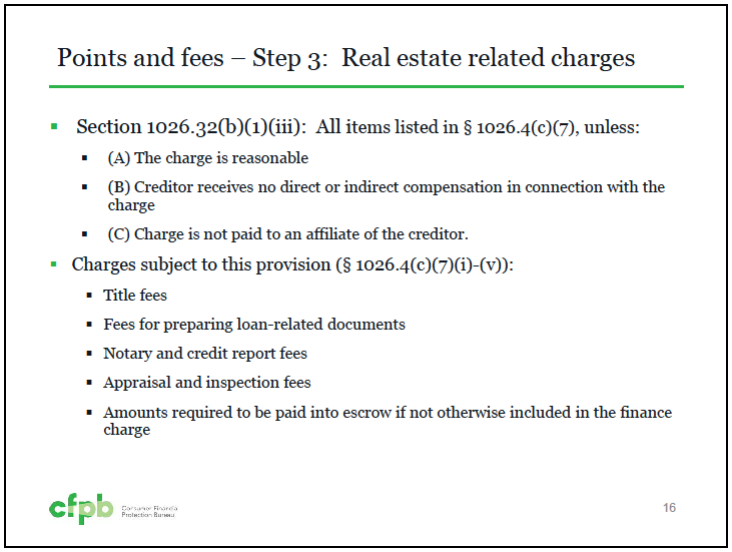
One, compensation paid by a consumer to a mortgage broker, as defined in § 1026.36(a)(1), and already has been included in the points and fees, in the points in fees under paragraph 32(b)(1)(i) This basically says, if there's loan originator compensation that was brought in to points and fees through the finance charge, you've already included it, you don't have to double count it. You don't have to include it again here. That was, I believe, finalized in May of this year.

Likewise, the second two prongs here, compensation paid by a mortgage broker to loan originator that is an employee of the mortgage broker and the same thing for a creditor, means that even if, you know, some how you could find compensation, meaning, you know, salaries or something like that, that a creditor or a broker is paying to its employee, that would meet the definition of loan originator compensation, that you don't need to include that and recently there

was a final rule that we put out in September, which I believe was published October 1st. We extended the same treatment to employees of retailers of manufactured homes. So that's one loan originator compensation. I know there were a bunch of questions about that, but I believe they've mostly been answered through amendments. So we can move on to the next step.



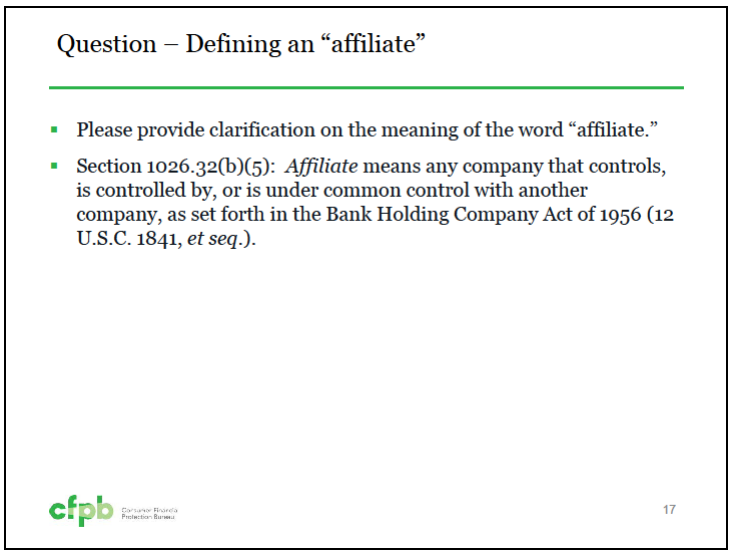
This is real estate related charges. So, you know, as you're probably aware, there are exclusions in § 1026.4(c) for certain things from the finance charge. What § 1026.32(b)(1)(iii) does is bring some of those items back in. The items that are listed in § 1026.4(c)(7) which are, you know, commonly referred to as "real estate related charges."



For your convenience, I've listed them out here, just so you can see what sort of charges we're talking about. We've got title fees, we've got fees for preparing loan-related documents, notary and credit report fees, appraisal and inspection fees, the amounts required to be paid into escrow

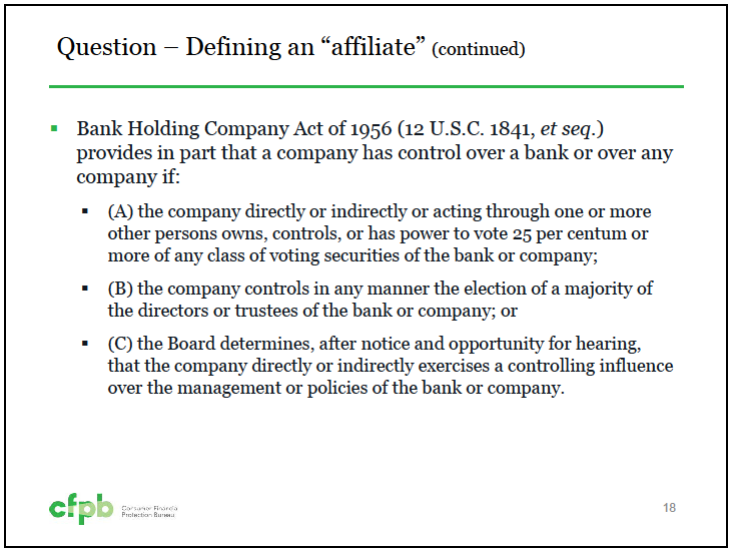
if not otherwise included in the finance charge. So these, the way § 1026.32(b)(1)(iii) works is these items are included unless (A) the charge is reasonable, (B) the creditor receives no direct or indirect compensation in connection with the charge, and (C) the charge is not paid to an affiliate of the creditor.

And we haven't gotten, really, it doesn't seem to be much of an issue, in the first prong, whether or not the charge is reasonable. We haven't gotten a lot of inquiries on the second prong either, but something that we have gotten a good deal of questions about is the, is the third prong, whether the charge is paid to an affiliate of the creditor. And now we'll talk about those specific questions.



LISA APPLEGATE: Indeed, and to start off, one question that we get frequently and we thought would be useful to answer here is, what is an "affiliate"? Please provide clarity on the meaning of the word "affiliate" in this context.

ANDY ARCULIN: Okay. So, the term "affiliate" is something that we have given a definition to in the rules. It's not new. It actually previously was intentionally fixed [inaudible]32(b)(2). When the new rules are finalized, or actually, you know, when Regulation Z is formally amended and becomes effective in January [inaudible] and that says that "affiliate" means any company that controls, is controlled by, or is under common control with another company, as set forth in the Bank Holding Company Act of 1956. So, we can go to the next slide.



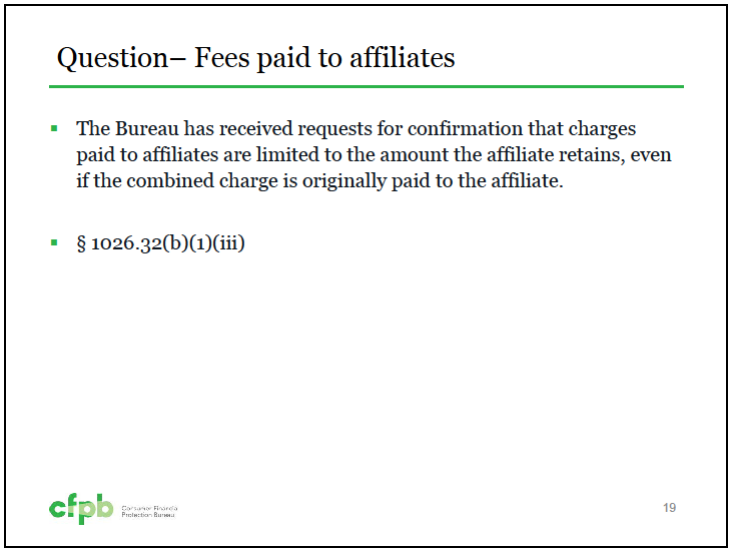
What I've done here is just sort of give you the relevant text of the Bank Company Holding Act of 1956 that you would want to look at to determine whether or not, you know, a certain entity is a corporate affiliate. This is, the first two, you know, I think, are really basically straightforward mathematical calculations - the company directly or indirectly, or acting through one or more other persons owns, or controls, or has power to vote 25% or more of any class of voting securities of the bank or company, or the company controls in any manner the election of a majority of the directors or trustees of the bank or company.

So obviously, under our rule, if you meet either of those two tests, then the company is an affiliate. And likewise, if the third prong is met, as well, the company is an affiliate, and this is where things get a little bit tricky. The third prong is, the board determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a controlling influence over the management or policies of the bank or company. So if there's actually, you know, there's a couple of points here.

First, if there's actually a board determination, one way or the other on this provision, we would, in our view, we would consider that to be controlling for purposes of the points and fees test. Likewise, if you meet (A) or (B) that also would be controlling for purposes of the points and fees test. So if you go through, if you go through this exercise and you determine under (A) that the company at issue is an affiliate, then nothing further to do, then you basically are an affiliate for purposes of our rule. Same thing with (B), and same thing if you get to (C). And, you know, to the contrary, if you don't meet (A) or (B) and the board determines that you're not an affiliate, you could say you're not an affiliate for purposes of our rule.

Where this gets a little bit tricky is this, you don't meet (A), you don't meet (B), you don't meet (B) and there has been no determination under (C). So you know, what we can say about that is the Board, the Federal Reserve Board still has the authority to make these determinations, and if there is no determination made and (A) and (B) are not at issue, that is - we would advise you to contact the board and seek their guidance on how to proceed. It's not, that's not something the

Bureau can directly address because the Board simply has interpretive authority, [inaudible] but I would also just throw out that, you know, there's no – at least for purposes of this rule, there wouldn't be any sort of consequence for treating a company that may be an affiliate, as an affiliate for purposes of these rule.



LISA APPLEGATE: Okay, let's stay on the topic of affiliates and move on to fees paid to affiliates. The Bureau has received many requests for confirmation that charges paid to its affiliates, are limited to the amount the affiliate retains, even if the combined charge is originally paid to the affiliate.

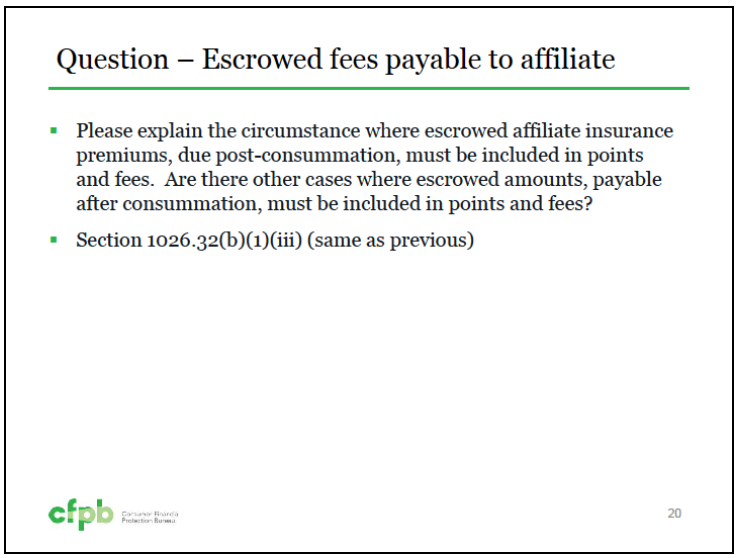
ANDY ARCULIN: Okay, so this is something that has come up quite a bit, and it commonly, to give you just an illustration, and I'm sorry, I don't have it on the screen for you, but I think it will be easy enough to follow. The most common illustration of this rule that I've heard is, the creditor has an affiliated appraisal management company - an AMC. And a charge is paid to the AMC, say its $500 to do an appraisal, but the AMC itself doesn't do the appraisal, the AMC itself hires an appraisal company that actually is an independent, unaffiliated third party to do the appraisal and pays that non-affiliate $400, but keeps $100 for itself. The question that has come up is, the $500 charge that's paid to the affiliate, meaning the money is handed to the affiliate and the affiliate essentially outsources the work, is that required to be included in points and fees or is only the piece that the affiliate keeps for itself required to be in points and fees?

This is, our reading of this rule is that, generally "paid to," means a person that is the ultimate recipient of and retains the charge. You know, I would also just note that it doesn't matter, under these rules, who pays it, as long as it's not the creditor. If you know, there's no requirement that the consumer has to pay this charge, it simply just says "paid to." But that's sort of an aside. What matters is that, you know, for purposes of our interpretation of this rule, the portion that's retained by the affiliate is what would need to be included in points and fees. So under the example I gave, you have, if you have $500 that's sent to an affiliate, but $400 is actually, you know, assuming that the charge is reasonable and there's no compensation paid in connection

with it, just to make sure we're covered there, the $400 is to a third party that's not affiliated and the charge wouldn't be included anywhere else, in our view, only the $100 retained by the affiliate would be included in points and fees.

LISA APPLEGATE: Okay, great. Thanks, Andy.

ANDY ARCULIN: No, wait, but one more point just to throw out, and, and you know, this also, just to let people know, because this has come up in other context too, this doesn't include general costs of business that are not specific to the transaction. So, in, in other words, an affiliate can't offset, you know, the amount that it retains. In this $100 example, the affiliate couldn't offset that amount by $20 in overhead that is not related to the transaction and say that it only really retained $80. It really is the amount retained, okay.



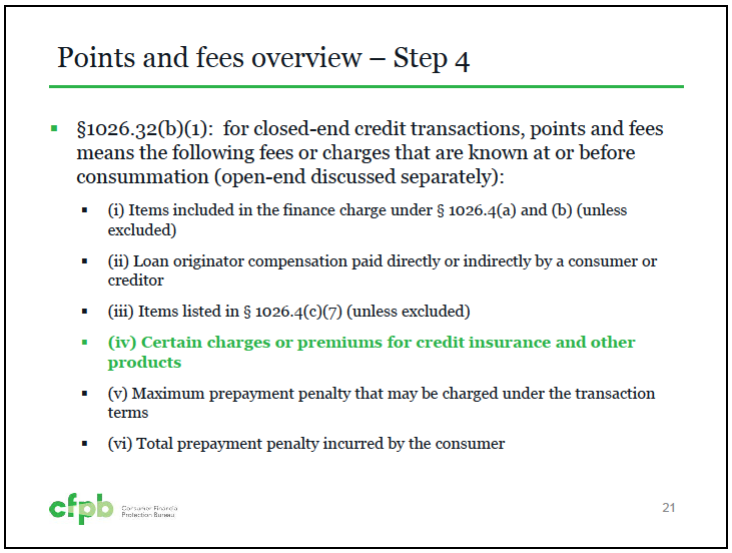
LISA APPLEGATE: Good clarification. Sticking with the topic of affiliates, on the next slide, please explain the circumstance where escrowed affiliate insurance premiums, which are due post consummation, must be included in points and fees. Are there any other cases where escrowed amounts, payable after consummation, must be included in points and fees?

ANDY ARCULIN: So, I mean, here, just to be clear, we're talking about amounts that are required to be put into escrow upfront, but, you know, they're being escrowed to be paid later. So as we talked about before, 23(b)(1)(iii) (sic – appears to reference "32(b)(1)(iii)") includes in points and fees all items included in (c)(7) unless among other conditions and charges, they're not paid to an affiliate of the creditor, among other things. If an amount is placed in escrow at consummation, but if one of these, you'll notice if you go back and look at § 1026.4(c)(7)(v) amounts required to be paid into escrow at consummation are not otherwise included in the finance charge, are included in (c)(7). So if that amount is payable to an affiliate, then it would be included in points and fees, even if it's put into escrow. It wouldn't matter that it's being put into escrow upfront versus just being paid.

So an example of this would be an initial escrow deposit for homeowner's association dues that, you know -

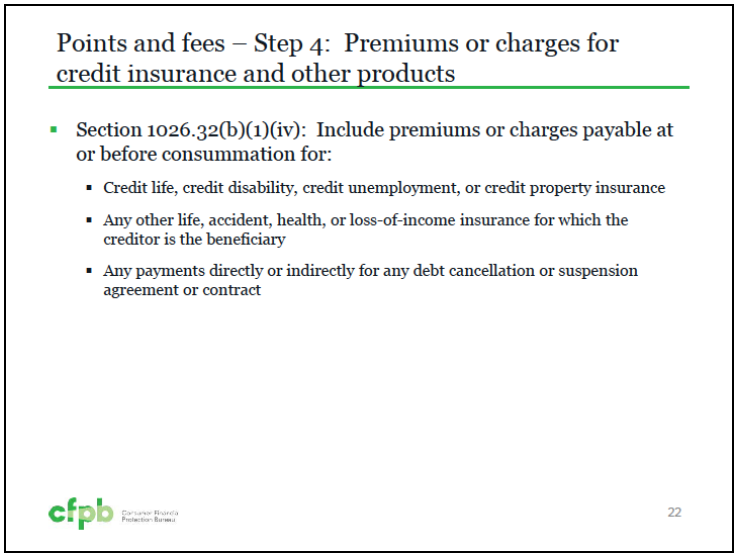
LISA APPLEGATE: **Homeowners' insurance?**

ANDY ARCULIN: Right, yes, right. Homeowner's as well. HOA dues is one, you know, if somehow they're in an affiliate relationship, if it was payable to an affiliate because, you know, those dues are not part of the finance charge, but, you know, something like an additional, an additional initial escrow deposit for mortgage insurance, that if it's included at all would be captured under the finance charge, would be captured there and not under this provision.



LISA APPLEGATE: **Okay, alright, let's move forward and get through the next aspect of the points and fees test.**

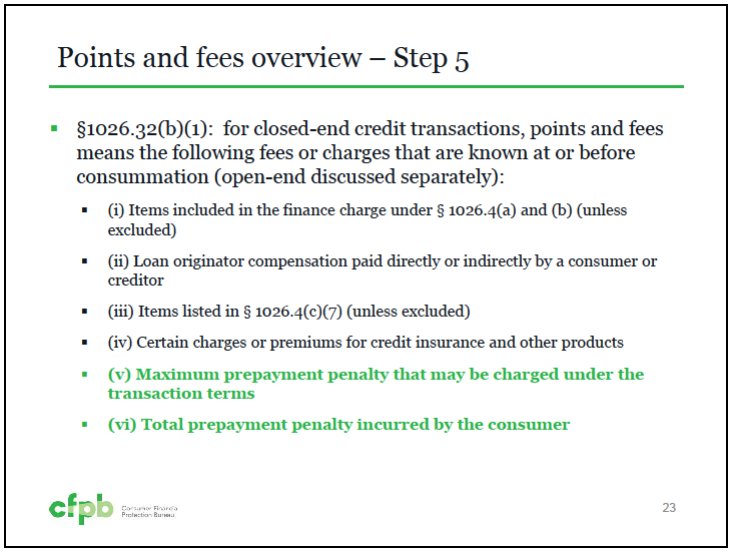
ANDY ARCULIN: Okay, so I think that, you know, that covers most of the interpretive questions that we've had about points and fees. You know, I'll still very quickly walk through the remainder of the test. The next step, go to the next slide.



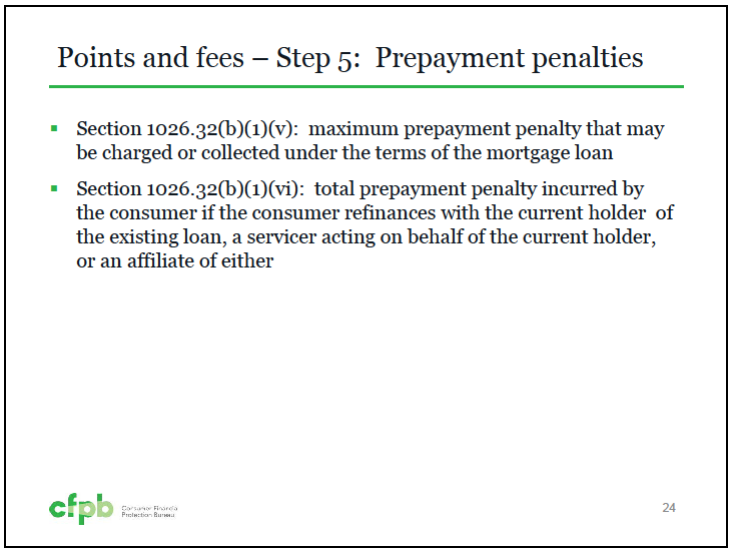
The next step is essentially for credit insurance premiums or charges that are paid up front. This is just really, you know, this is an abbreviation of the regulation text, you know, to the extent that this is an issue, just look at 32(b)(1)(iv) premiums or charges payable at or before consummation for credit like, credit disability, credit unemployment, or credit property insurance, any other life, accident, health, or loss-of-income insurance for which the creditor is a beneficiary and any payments directly or indirectly for any debt cancellation or suspension agreement or contract. And the only thing that I would note there is, you know, you would also, just for your benefit, want to you know, pay attention to the prohibition on creditors financing credit insurance which is in the loan originator compensation rule to make sure you're not running into that rule. This is something different, I'll just throw that out there, you know.

LISA APPLEGATE: Okay, next one.

ANDY ARCULIN: Next slide.

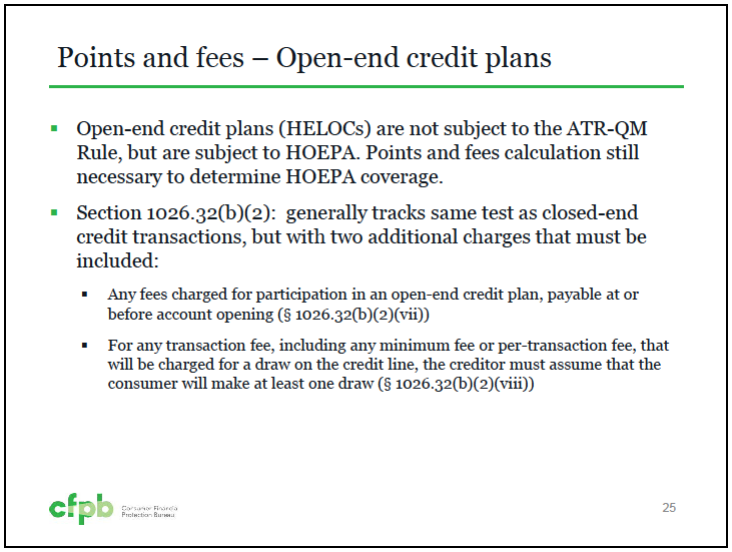


LISA APPLEGATE: **One more.**



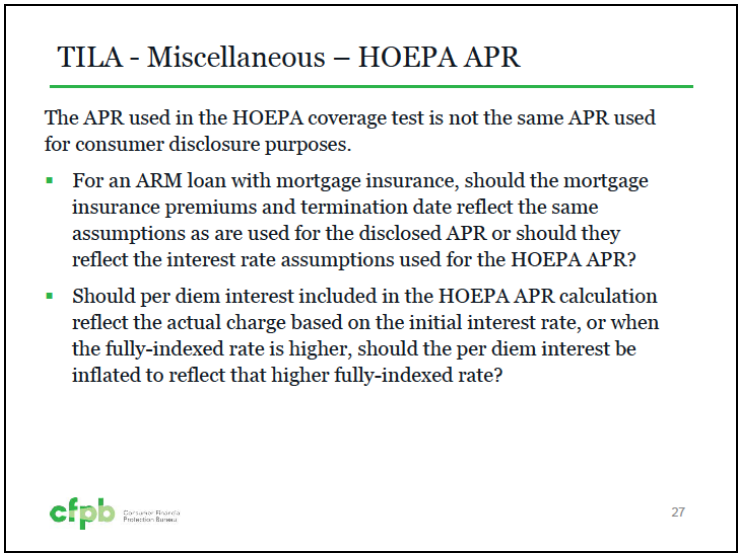
ANDY ARCULIN: These are the last, the last two are, you know, basically about prepayment penalties that would be included. Again, these are not areas where we've received a lot of questions. I just sort of put them up there just so we're walking through the whole test. First one, the maximum prepayment penalty that may be charged or collected under the transaction terms; that's a prepayment penalty that you could pay under the terms of the mortgage. The second one is the prepayment penalty that is actually incurred, if you refinance an existing mortgage with the current holder or servicer acting on behalf of or an affiliate.

So that's points and fees for closed-end. We can go to the next slide.



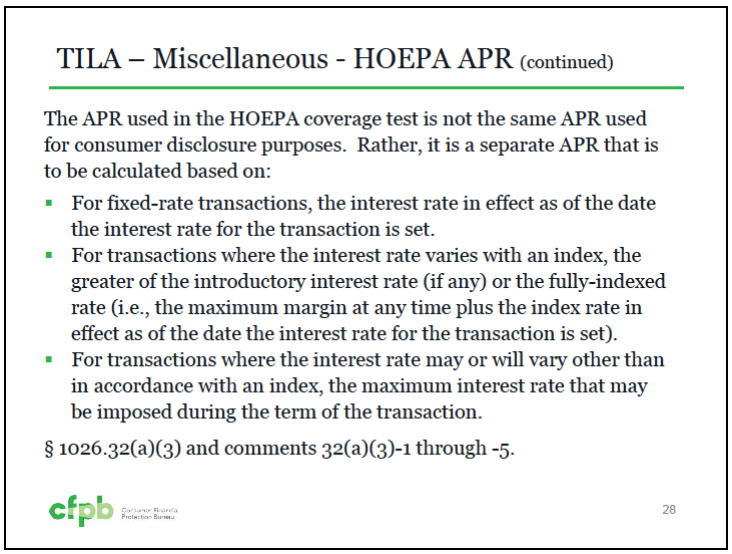
This next slide is basically, you know, again, we won't spend a lot of time on this but this is just to illustrate that there's also points and fees for HOEPA coverage that applies to HELOCs to the extent you're making HELOCs you would want to go through this test to make sure, you're within the points and fees test set forth in HOEPA and the actual rules are set forth in § 1026.32(b)(2). It generally tracks the same test as closed-end credit transactions with some nuances. You'll, you'll see that the closed-end rules typically refer to the consummation, whereas, you know, these open-end rules will refer to account opening because you're talking about a HELOC versus a closed-end loan. There's some differences like that. Otherwise, there's really only two provisions that are specific to HELOCs – one is prohibited fee charge, participation in an open-end credit plan payable at or before account opening. That's just a participation fee in the plan that's paid up front. And the second one is if there's a transaction fee. Basically, if there's a fee that's charged per draw, the creditor would have to assume that the consumer will make at least one draw and include that in points and fees. So that is points and fees.

LISA APPLEGATE: Okay, well thanks, Andy for that marathon. All right, moving on, we have a few inquiries we are going to cover, from various places within Reg. Z - TILA and we're going to start with the HOEPA APR. We've received a number of inquiries about how the HOEPA coverage test APR and the consumer disclosure APR interact. They are not the same. Which do you use when?



So, for example, for an ARM loan, with mortgage insurance, should the mortgage insurance premiums and termination date reflect the same assumptions as are used for the disclosed APR or should they reflect the interest rate assumptions used for the HOEPA APR? Should per diem interest included in the HOEPA APR calculation reflect the actual charge based on the initial interest rate or, when the fully indexed rate is higher, should the per diem interest be inflated to reflect that higher fully-indexed rate? Nick, can you walk us through this?

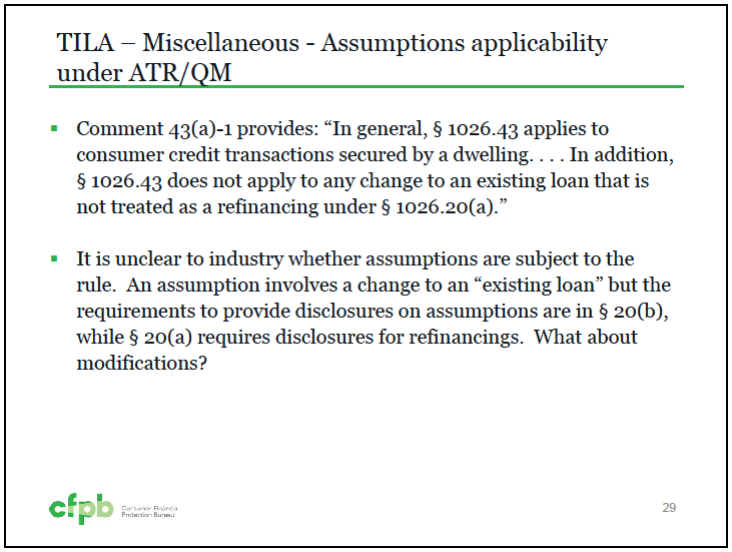
NICK HLUCHYJ: Yes, thank you, Lisa. I can. Good afternoon, everyone. I think this is a fairly complicated question. We may toggle back and forth between these two slides for this purpose. The interest rates, for purposes of making the HOEPA determination, is set by both statute and regulation at a different level then you would use for purposes of the disclosed APR. And it allows, or establishes, a base rate that's used for purposes of determining what the APR will ultimately be. Now as you can see from this slide, three different situations are covered, fixed rate, that's pretty straight forward, it's just the interest rate for the transaction. We have an ARM - the interest rate varies with the index – it's the fully indexed rate and that's the index plus the maximum margin. And then, where the interest rate may vary but other than within index, say a step loan, it's the maximum interest rate. Now, the result of this, is that the APR for purposes of the HOEPA determination, the base rate that is, may often be, frequently will be higher than the base rate that's used for purposes of the disclosed APR. There are other elements that are factored into the determination of what the final APR will be and these other elements are frequently influenced or their outcome levels which they are finally set, will be definitely affected by the base interest rates to which they're applied.



Now, an example of this would be the mortgage insurance premium. The Homeowner's Protection Act establishes the cancellation for the mortgage insurance premium when the loan reaches 78% LTV. Now, the calculations for when that happens, that is, at which payment will the loan reach that 78% LTV will differ and it will take longer with the higher interest rate then with the lower interest rate. And the impact of that is, that it's, you'll use a higher interest rate to determine this factor for determining what your final APR is. You're going to wind up with a higher APR then if you use the interest rate that's used for purposes of the disclosed APR.

We believe, it's our opinion that the interest rate that's used for the disclosed APR should be used for purposes of determining the mortgage insurance premium drop off date. So, whatever level that comes in at, would then be applied with respect to the HOEPA rate. So you do the determination, of what the element applied to the APR is, the base APR, but that element that's applied to the HOEPA rate is determined the way it is always determined, up to this point. The

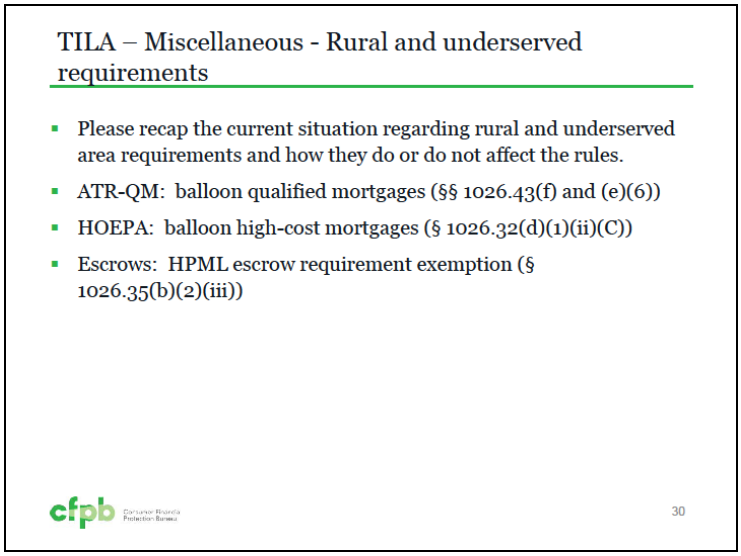
same would be the case with respect to the per diem interest charge. You would calculate it to reflect the actual charge that's based on the initial interest rate and then whatever that amount is, would be applied to that base rate that is derived from the HOEPA APR calculation. That's the model that should be used.



LISA APPLEGATE: Okay, well thanks very much. Alrighty, let's switch gears and talk a little bit about assumptions applicability under ability to repay and qualified mortgage rule. So comment 43(a)-1 provides, "In general, § 1026.43 applies to consumer credit transactions secured by a dwelling. . . In addition, § 1026.43 does not apply to any change to an existing loan that is not treated as a refinancing under § 1026.20(a)." It is unclear to industry whether assumptions are subject to the rule. An assumption involves a change to an "existing loan," but the requirements to provide disclosures on assumptions are in section 20(b) while section 20(a) requires disclosures for refinancing. And what about modifications? Can you shed some light, Nick?

NICK HLUCHYJ: Yes, thank you, Lisa. This also is a question that requires some background explanation. Even though assumptions are under 20(b) and are not explicitly addressed in the rule, which only refers to 20(a), we believe that since they are subject to the disclosure requirements, that they should be considered new transactions for purposes of the ATR/QM rule. Now the important consideration here, or an important consideration, because there are several, is that, in order to have an assumption, one of the express provisions in § 1026.20(b) is that the assumption occurs only when the creditor expressly agrees in writing to accept the subsequent consumer and so if that does not occur, there's not an assumption, for purposes of section 20(b) and therefore, there would not be a new transaction for purposes of the ATR/QM rule. Now with respect to modifications, a modification does relate back to the refinancing definition under 20(a) and there's a refinancing when there's a satisfaction of the original obligation and creation of a new obligation.

Now, if the transaction does not involve satisfaction of the original obligation and creation of a new one, it qualifies as a modification. In the context of an assumption, the modification may take place at the points of the assumption transaction itself. So if the assumption and the modification take place at the same time, as a single transaction, the terms that are used following modification, should be used for purposes of the ATR/QM determination. On the other hand, if the assumption takes place first and the modification is postponed to determine whether the new creditor or the new consumer qualifies, then the ATR/QM determination is made on the basis of the terms that would apply only under the assumption.



LISA APPLEGATE: Okay, alright. Switching gears again. We thought it would be a good idea to recap the current situation amongst the ATR/QM, HOEPA, and escrows rules as it relates to rural and underserved area requirements and how they do or do not affect the rules. Andy, can you go over that?

ANDY ARCULIN: Sure, so we have, there's a definition of rural and a definition of underserved that are both, they were finalized as part of the escrows final rule and they're in § 1026.35(b)(2)(iii). Some parts of that provision, there's three rules that are affected. Basically, "rural" is given a meaning under these provision, based on UIC [(Urban Influence Codes)] codes, that are published by the U.S. Department of Agriculture, their Economic Resource Service. And "underserved" is given a meaning based on HMDA data, for particular counties. Both of these are county wide determinations. So there's three different things you should know about just to sort of give you a foundation on rural and underserved. There's the, an HPML escrow requirement that's generally any higher priced mortgage loan is required to have an escrow unless it meets certain exemptions, one of which is the creditor operates predominately in a rural or underserved area. And there's some other requirements as well. There's also a provision in the ATR/QM rule that's § 1026.43(f) that allows for some creditors, who meet certain small creditor criteria, to make loans that meet other criteria also set forth in 43(f) if that creditor operates predominately in a rural or underserved area.

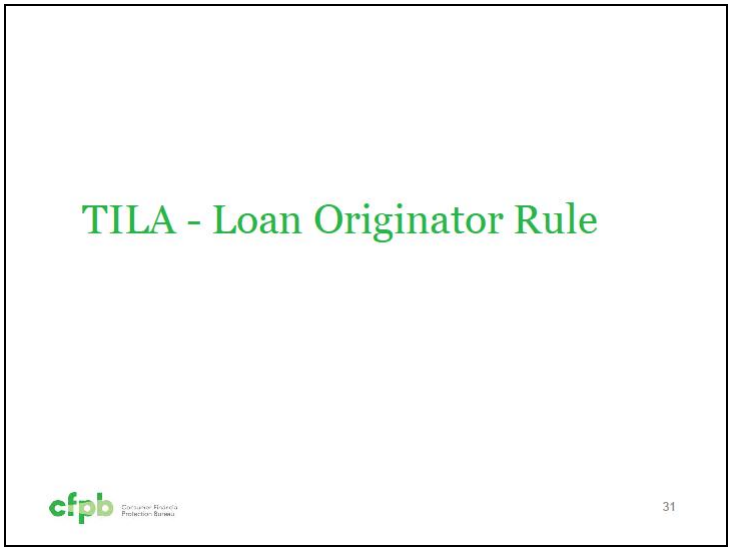
And then based on that, there's also a provision in HOEPA, which is in § 1026.32(d)(1)(ii)(C) that allows for some high cost mortgages to have balloon features if those loans and those creditors meet the criteria set forth in § 1026.43(f). Essentially, these are loans that meet the qualified mortgage standards for balloon QMs and the creditors also meet these certain small creditor criteria set forth in the rule. That's all just kind of background, so you can follow where I'm going. What's happened since these rules came out, we've, the Bureau has basically decided that in the next two years we intend to re-examine the definitions of "rural" and "underserved" that we've adopted that would obviously affect these three rules. There's several reasons for that which, you know, essentially, you know, the definition of "rural" is based on these UIC codes that are only updated with the most recent census and, you know, there's also just some nuances to those determinations that, you know, if you really get into counties, you know, in Mountain West, that are very large, that a corner of the county touches on the commuting pattern or something like that, the county may not be considered rural under our rules.

We've decided just to go back and look at the definitions and either stick with them or change them, based on that evaluation. So in the meantime, we've done a couple of things to facilitate credit by small creditors. One is to the ATR/QM rule. We have § 1026.43(f), which is still there, which I just covered, basically allows for some, some balloon loans to be made as qualified mortgages, if the creditor meets various small creditor criteria and the loan also meets criteria. What we've done is we've adopted, through the ATR/QM concurrent final rule, which was published in May, provision § 1026.43(e)(6), that keeps the same test intact, except for the fact that the creditor does not need, no longer needs to satisfy the operating predominately in a rural or underserved area requirement for the next two years, with the caveat that provision sunsets on January 10th, 2016.

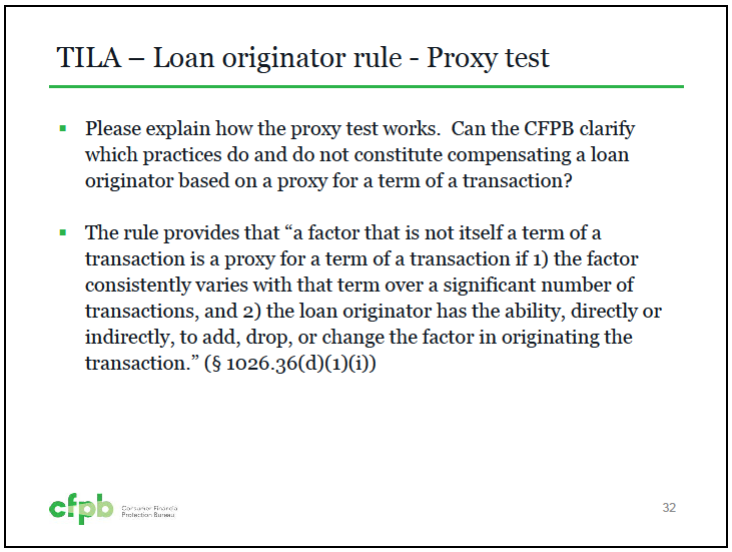
For HOEPA, we recently, and in the final rules that we just published October 1st, we basically, because this provision more or less piggy backs off of 43(f), we've added (e)(6) to it. So for HOEPA, a small creditor that satisfies, that makes a loan that satisfies (e)(6), which means satisfies 43(f) in every respect except for the operating, the creditor operating predominately in a rural or underserved area, then a high cost mortgage can be made as a balloon loan.

And then finally there's the HPML escrow requirement. We did not go and, you know, essentially remove the rural or underserved requirement for the next two years, like we did for the other rules for that exemption. What we've done there, is we've basically said because largely because the UIC codes are dependent on the census, what happened was, after the most recent census came out, you know, a good number of counties would have been removed from eligibility as a rural county and, you know, some number also would have changed as underserved counties as well. And, in order to allow those creditors who were sort of, you know, they had just gotten started, they were operating under the presumption that they were eligible for this exemption from the escrows requirement to allow them to keep it going forward while we re-examined those definitions, we've gone and we've said, you know, that the way that the HPML escrow requirement exemption works is the creditor has to have operated predominately in a rural or underserved area in the previous calendar year, meaning, you know, more than half of their loans in the previous calendar year were made in counties with the rural or underserved definition. What we've done is we've allowed them to look back for three years. So a creditor

who qualified this year, because the rule became effective in June for the exemptions, will not lose it next year because of some change in the county's status based on the census. That creditor can continue to take advantage of the exemption for the next two years, while we're re-examining the definitions and on top of that as well, you know, it didn't penalize someone, who, because their county was added to a rural county list from taking advantage of the same exemption



LISA APPLEGATE: Okay, great, thank you very much. Much appreciated. So now we're going to take another twist in the road, and move around to the loan originator rule and discuss a few questions with Dan. So the first FAQ is, is regards to the proxy test.



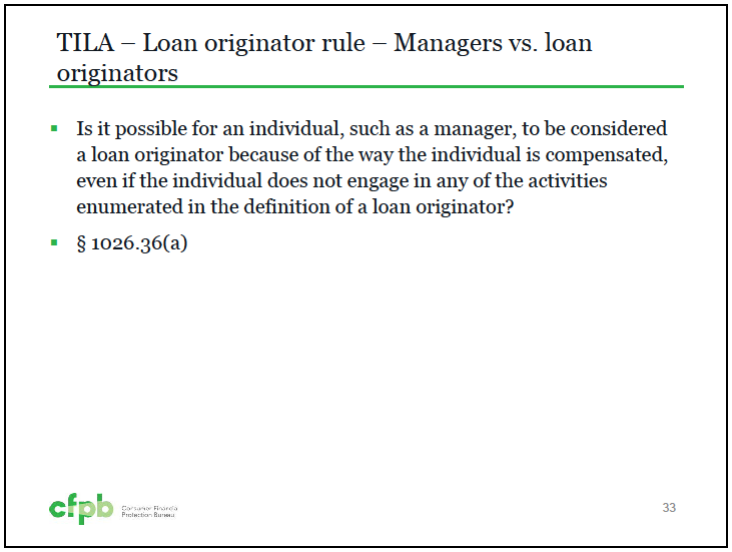
You know, please provide an explanation of how the proxy test works. Can we clarify which practices do and do not constitute compensating a loan originator based on a proxy for a term of a transaction?

DAN BROWN: Thank you, Lisa. As background, first, I just wanted to point out that the loan originator rule prohibits loan originator compensation that is based on a term of a transaction or on a proxy for a term of a transaction. That prohibition was in the Federal Reserve Board loan originator rules, but the CFPB, in their January rule provided a test or definition of "proxy" that wasn't in the rule previously. So first of all, let's go over the test itself. The rule provides that a factor that is not itself a term of a transaction is a proxy for a term of a transaction if (1) the factor consistently varies with that term over a significant number of transactions, and (2) the loan originator has the ability, directly or indirectly, to add, drop, or change the factor in originating the transaction.

So, to answer this question, first, I want to start out by pointing out that both prongs of the proxy test are highly dependent upon particular facts and circumstances, and that those facts and circumstances for a particular transaction are going to be best known by generally by the persons who are paying and receiving loan originator compensation that is subject to the rule. So a given factor may vary consistently, with loan terms, in some cases, but not in others. And a loan originator may be able to add, drop, or change a factor under certain circumstances but not under other certain circumstances. Accordingly, when we get these questions, and we do get a lot of questions about whether particular factor is or isn't a proxy, we generally are not able to provide a definitive answer or guidance about whether a given factor is always a proxy, sometimes a proxy, or never a proxy. It really depends on the facts and circumstances of a particular transaction.

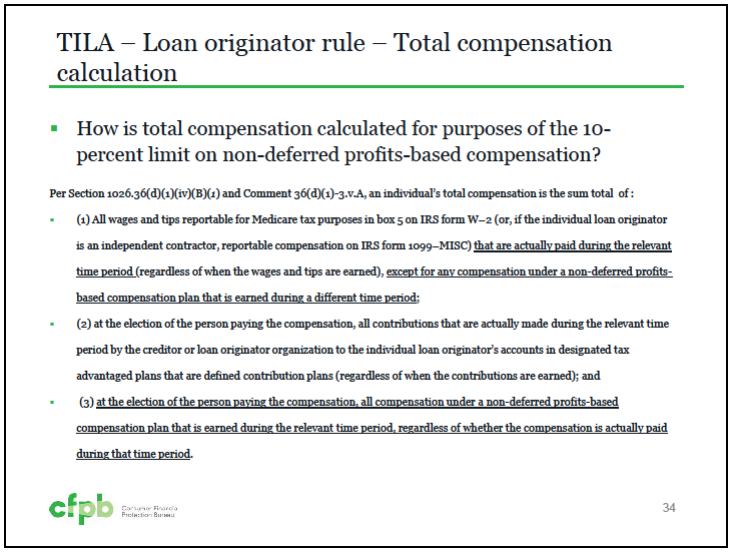
So we can provide an illustration. So to illustrate, the proxy test could be applied to determine whether a factor such as the location of a property that is going to secure a loan is a proxy for a loan term. So for purposes of this illustration, let's assume that loans secured by properties in state A generally have higher interest rates than loans secured by properties in state B. In this case, the first prong of the test appears to be met. However, if the loan originator has no ability to influence whether a transaction is secured by a property in state A or state B, as one normally might expect, then, the second prong of the proxy test is not met, and the location of the property would not, in this case, be a proxy for the term of the transaction.

However, just to counteract that, if, on the other hand, the loan originator serves consumers in a particular metropolitan area that includes states A and B and it so happens that it is possible the loan originator can, under some circumstances, influence a consumer to purchase a property that will secure the loan in one state rather than the other. Then, in that case, the property in which the, the state in which the property is located would be a proxy for the term of the transaction. So under those particular circumstances, compensating a loan originator based on the state in which the property is located would be prohibited under the rule.



LISA APPLEGATE: Okay, great, very customized determinations on the proxy test. Thanks, Dan. Sticking with the loan originator rule, let's talk a little bit about managers versus loan originators. Is it possible for an individual, such as a manager, to be considered a loan originator simply because of the way the individual is compensated, even if that individual does not engage in any of the activities enumerated in the definition of a loan originator? Dan?

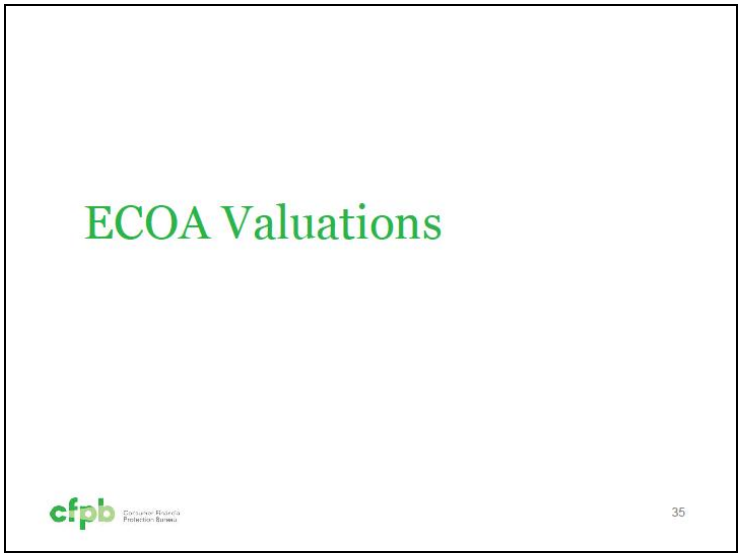
DAN BROWN: So the basic answer to this question is no. And that is because the definition of loan originator in § 1026.36(a) provides that to be a loan originator, a person must engage in one of the enumerated loan origination activities for compensation or gain or in expectation of compensation or gain in order to be a loan originator in the first place. So for purposes of this question, we very often get this question with respect to managers. The key here is that management itself is not an activity that is among the enumerated loan originator activities. So therefore an individual does not become a loan originator merely because that individual manages other people who are loan originators. So, to take that further, the way in which a person, that is a manager, is compensated cannot cause a person who is not otherwise a loan originator to become a loan originator, that is, if that person does not perform any of the enumerated loan originator activities. Of course, if the person does engage in at least one of the enumerated loan originator activities, and the person is compensated for those activities, then the person is a loan originator, without regards to how that person is compensated. In that case, then the person's compensation is subject to the loan originator compensation rule.



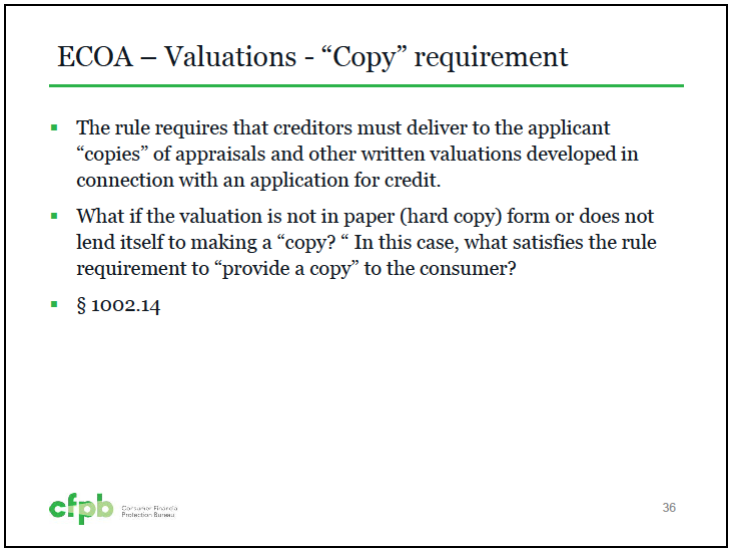
LISA APPLEGATE: Excellent, thanks very much. Last question related to the loan originator rule. Total compensation calculation - can you go through how the total compensation is calculated for purposes of the 10% limit on the non-deferred profits based compensation?

DAN BROWN: Sure, so the CFPB's January final rule permitted payments of compensation to an individual loan originator under a non-deferred profits based compensation plan if the non-deferred profits based compensation does not exceed 10% of the individual loan originator's total compensation. The Bureau's September final rule, or the one published in the Federal Register on October 1st, clarifies some important details about how to calculate an individual's total compensation. In particular, that recent rule provided additional detail on what items must be excluded and what items may be included in total compensation at the election of the payer of the compensation. That rule addresses components that are counted based on when they are paid to the loan originator, and which other components are counted based on when they are earned.

So I won't torture people by going into, by reading the entire formula, but it is on the screen, the slide here. So I would call people's attention to the text that is underlined on the slide. The underlined text is that which was changed recently. These changes, generally speaking, we think are relatively minor in substance but to provide greater clarity on how to determine how much non-deferred compensation may be paid under the rule. Even though these are relatively minor substantive changes, we do think it was important to note them here because we think it will be helpful for anyone who is currently making changes to compensation plans in anticipation of the January effective date, since in the end this is ultimately a math, a mathematical equation. So in the end, there is a right and wrong answer so we just wanted to draw people's attention to the exchange.



LISA APPLEGATE: Okay, great. Okay, so that concludes our tour of FAQs related to TILA. Now we're going to cover a question related to ECOA. In the valuations rule, under the "copy" requirement, the rule requires that creditors must promptly deliver to the applicant copies of appraisals and other written valuations, which are developed in connection with an application for credit.



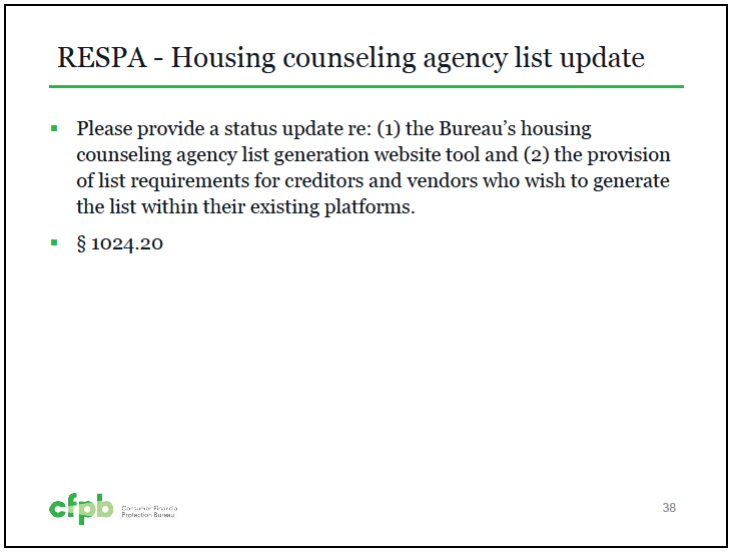
Nick, what if the application is not in paper or hard copy form, and does not really lend itself to making a "copy"? In this case, what satisfies the rule requirement to "provide a copy" to the consumer?

NICK HLUCHYJ: Thank you, Lisa. This is an example, if I may stray off a little off topic of . . . Once upon a time this never would have been an issue, never would have been a question, but technology is, as often observed as a blessing and perhaps not a blessing. I don't want to go so

far as to say it's something else but in this instance, it becomes difficult at times to determine, in the case of say, electronic records, where an AVM, an automated, automated valuation model, is being used, the records or the data that's produced is oftentimes not differentiated into discreet units that easily present themselves for purposes of making a copy to give to the consumer because they may contain unrelated information, proprietary information, things that would not be appropriate to include. The guidance we provide on this subject when it comes in, and people do ask, is that the, at a minimum, and really the minimum is what's required, is that you have to provide at least the estimated, estimated home value, so that has to be in there, plus the data that was relevant in arriving at that estimated value including information related to how the calculation is made. The idea is to present the consumer with both a sense of what the value is, and how that value is determined and so now in terms of how that copy is presented, it doesn't have to be a paper document. The rule explicitly provides at § 1002.14(a)(5) that an electronic copy may be provided.

Now, if subsequently you develop an additional appraisal or estimate of value, based on that data that you have from your AVM, and it differs, you would be required to provide that copy conforming with the previous requirements, also, to the consumer. Thank you, Lisa.

LISA APPLEGATE: Okay, great. Alright, last, last update. This one is RESPA.



LISA APPLEGATE: **Andy, can you please provide folks with a status update related to the Bureau's housing counseling agency list generation website tool, and also the provision of list requirements for creditors and vendors who wish to generate the required list within their own existing platform?**

ANDY ARCULIN: Okay, so the regulatory site there is just to remind, I mean, my answer doesn't really relate directly to that. That's just where the requirement is found that this list of counseling resources will be made available, you know, basically be [inaudible] loan. But, you know, in terms of the status of the website that we're building and the data capability that we're also working on, we expect to release both the website for housing counselor agency list generation and the specifications for creditors who want to build the list generation functionality into their own systems in the coming months. So you know, two things, in one week, we're going to have the website released in the coming month. We're also going to have specifications for creditors who want to do this data link capability on their own in the coming month as well. Obviously, we're not going to expect that, that the specifications will be fully built and implemented by January, so, and we realize that many of you plan to build the list functionality yourselves and you'll need programming time so we will be providing an interim path for compliance. As to what that will be, I would just say to stay tuned, that that will also be released in the coming months.

LISA APPLEGATE: Excellent, alright, thank you, Andy. So that wraps up the FAQ tour for today's session on the origination rules. As Dave mentioned earlier, on this slide, just recapping, a lot of you are aware of this, there is always the ability to ask questions regarding the meaning or intent of CFPB regulations, these rules, and any others at the email address and phone number on your screen. CFPB_reginquiries@CFPB.gov or (202) 435-7700. It won't be the case that the person that picks up the phone will be able to answer your question, but your calls will be routed and responded to within several business days and you will be talking with an expert. So this was not the "be all, end all" of all questions that you may ever be able to ask. I also wanted to draw folks' attention to the fact that there is a lot of focus at the Bureau on regulatory implementation for these rules and providing support tools for folks around the content, reference materials, pulling all of the various rules and updates into one place and that website that you see printed there, consumerfinance.gov/regulatory-implementation is where you can find quite a trove of resources if you're not already aware of it. I encourage you to visit. So with that, I think that concludes today's session. I want to thank the MBA for hosting us, and I want to thank all of you for keeping up. I'm sure as best as you could I think a recording will be produced and made available of this session so for folks who want to drill in on specific questions, you'll be able to slow it down a little bit and take it in maybe a little more easily then you were able to today. We appreciate everyone's time and effort and diligence in implementing these rules. We know it's a huge list, and we want to do anything we can to help out. Thanks so much and thanks to the MBA.