

**SCHWARTZ & BALLEN LLP**

1990 M STREET, N.W. • SUITE 500  
WASHINGTON, DC 20036-3465

(202) 776-0700

FACSIMILE  
(202) 776-0720

www.schwartzandballen.com

**MEMORANDUM**

July 15, 2008

To Our Clients and Friends

Re: Federal Reserve's Regulation Z Residential Mortgage Rule

The Federal Reserve has issued a final rule under Regulation Z, Truth in Lending, prohibiting unfair or deceptive home mortgage lending practices. The rule also establishes required disclosures and advertising standards for closed-end mortgages. The rule is effective October 1, 2009.

The rule applies to loans that meet HOEPA<sup>1</sup> cost triggers and "higher-priced mortgage loans,"<sup>2</sup> which are defined as closed-end loans secured by a consumer's principal dwelling where the annual percentage rate on the loans exceeds the average offer rate on prime loans published by the Federal Reserve by at least 1.50 percentage points for first-lien loans or 3.50 percentage points for subordinate-lien loans.

The rule prohibits the following four practices:

- Extending credit based on real estate collateral without regard to the consumer's ability to repay from income or assets other than the value of the real estate
- Making a loan without verifying the income and assets relied upon to determine the consumer's ability to repay

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<sup>1</sup> Home Ownership and Equity Protection Act (HOEPA) loans are closed-end, non-purchase mortgage loans where either the annual percentage rate exceeds the yield on Treasury securities of comparable maturity by more than 8 percentage points for first-lien loans or 10 percentage points for subordinate-lien loans, or the total points and fees payable exceed the greater of 8 percent of the total loan amount or \$547 for 2007.

<sup>2</sup> "Higher priced mortgage loans" are defined as closed-end loans secured by a consumer's principal dwelling where the annual percentage rate on the loans exceeds the average offer rate on prime loans published by the Federal Reserve by at least 1.50 percentage points for first-lien loans or 3.50 percentage points for subordinate-lien loans.

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- Imposing prepayment penalties if the payment can change in the initial four years of the loan. For certain higher-priced loans, a prepayment penalty cannot last more than two years
- Failure to establish escrow accounts for property taxes and insurance<sup>3</sup>

In addition, the rule also applies the following requirements to all loans secured by a consumer's principal residence:

- Creditors and mortgage brokers are prohibited from coercing an appraiser to misstate a home's value
- Mortgage servicers are prohibited from engaging in certain practices such as pyramiding late fees and failing to credit payments as of the date of receipt
- Creditors must provide a good faith estimate of loan costs, including refinancings and home improvement loans, within three days after a consumer applies for a mortgage loan

The new advertising requirements require additional information about rates, monthly payments and other features.

A copy of the Fed's rule can be found on our website at [http://www.schwartzandballen.com/whats\\_new.html](http://www.schwartzandballen.com/whats_new.html).

If you have any questions, please call Gilbert Schwartz, Robert Ballen, Tom Fox or Heidi Wicker at (202) 776-0700.

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<sup>3</sup> This provision is effective in 2010.