### Summary of Annual 2008 Committee Meeting

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### Newsletter of the ABA Section of Business Law Committee on Consumer Financial Services

#### Consumer Financial Services Committee 2008 Annual Meeting New York, New York

**Committee Program:** Those Lowdown Subprime and Credit Crunch Blues and What They Mean for Business Litigators - August 9, 2008

*Julie Rystad, Greenberg Traurig, LLP*

**Program Speakers:**

- **Professor Kathleen C. Engel,** Cleveland-Marshall College of Law, Cleveland, Ohio;
- **Douglas G. Duncan,** Chief Economist, Fannie Mae, Washington, D.C.;
- **Jayant W. Tambe,** Jones Day, New York, New York;
- **Charlotte Bahin,** Office of Thrift Supervision, Washington, D.C.

The program introduction emphasized how the subprime credit crunch has a far-reaching impact across industries. For example, it was a contributing factor to the recent layoffs at Cadwalader, Wickersham & Taft LLP, and other national law firms.

Mr. Duncan delivered a mortgage market update. The credit crunch in the mortgage industry has affected the general economy, and indications are that the mortgage industry downturn is not over. Although the housing market may be past the "inflection point" at which prices stop declining, there have recently been a half million or so layoffs that could prolong the housing market recovery. In normal times, housing price declines in specific markets typically last about 2 years. Mr. Duncan likened the mortgage and housing markets to a swimming pool, which is simultaneously being filled and drained. The "fills" are made up of 10-11 months of foreclosure inventory, new housing, existing home sales, and condo conversions. The swimming pool is simultaneously being "drained" by destruction, new home sales, existing home sales, existing home withdrawals, and apartment conversions. The drains are not currently keeping pace with the fills. With about 1 million excess capacity of homes, Mr. Duncan forecasted that the "bottom" might be reached in the fourth quarter of 2008, although it might be later in certain markets. For example, Florida could have five years’ worth of surplus properties. The worst "bubble states" may be California, Arizona, Florida and Nevada.

A recession might be pending, as recessions and housing market downturns have historically coincided with failures of a significant banking market.

As a result of the existing issues, lenders have tightened their underwriting criteria on all types of loans, whether subprime, prime, or Alt-A.

Unanticipated issues may also result from the fact that commercial interest rates have been very low for several years, which means that risk premiums were too low. The number of foreclosures as a percentage of delinquencies has been rising. This may be a result of products with 100% loan to value ratio, for example.

Mr. Tambe said that the mortgage industry credit crunch is causing "Radiating Ripples of Subprime Litigation." Mr. Tambe
reiterated that the mortgage industry downturn crosses all asset classes. It has affected markets outside the mortgage industry, including, for example, auction rate securities. Mr. Tambe likened the litigation trends resulting from the mortgage industry credit crunch to a "circle of claims" as follows:

1. mortgage origination  
2. securitization (RMBS)  
3. collateralized debt obligations (CDOs)  
4. shareholder and derivative claims  
5. other litigation (e.g., auction rate securities)

Mr. Tambe predicted that recent bank failures may be the precursor to "RTC Part II," meaning that more bank failures may be forthcoming and the government should be expected to intervene.

Mortgage defaults are the ultimate source of rising litigation related to securitizations. Mortgage defaults can cause securitization trusts to default on their obligations to investors. Since these trusts may not have sufficient capital to satisfy investor claims, investors may look to underwriters as the next group of defendants who "should have known" by due diligence that these mortgage loans were too risky. Investors might also target originators, although originators are often not sufficiently capitalized to be good litigation targets. Limited recourse may be obtained from them prior to litigation through repurchase obligations.

**Other litigation trends:**

There has been an increase in CDO litigation. Plaintiffs generally are institutional investors, banks, and pension funds, all of whom are suffering losses on AA- and B-rated investments. These claims relate to losses, disagreements over the priority of payments, and liquidation of assets. There is and will be more bank against bank litigation, litigation among hedge funds and fund investors, and litigation against monoline insurers.

**Who else is getting sued?** Everyone up the line. Expect law firms to be sued next.

**What are the claims?** Claims include sales practices, securities claims, breach of fiduciary duty, contract claims, and shareholder claims. Shareholder class claims against banks, monoline insurers and others. The general gist of the claims? Overexposure to risk.

**RTC Part II.** More bank failures are forecasted over the next 18 months. Expect 75-150 of them.

**Forum and venue issues.** For example, the Cleveland and Baltimore nuisance claims, a 1933 Act claim brought in California Superior Court, or Asian investors filing claims against U.S. companies in the Far East.

Ms. Engel spoke about trends in consumer litigation, including more claims regarding TILA disclosures, RESPA anti-kickback violations, unfair and deceptive practices, and, to a lesser extent, harder-to-prove fraud and unconscionability.

There have also been more FHA and ECOA discrimination claims alleging price discrimination based upon race, age or gender. Other claims arising from mortgage transactions include: RICO conspiracy, warranty, breach of fiduciary duty, "improvident lending" (a tort), and claims regarding servicing...
practices. "Structural unfairness claims”—essentially, claims that all the terms of the loan taken together were unfair to consumers, even if no specific term was illegal or unconscionable standing alone—are arising in the absence of express statutory prohibitions on lender’s practices.

Potential defendants in these types of claims can include brokers, appraisers, lenders, and title companies. They can also include "stretch defendants" such as underwriters, accounting firms, and rating agencies.

Other changes in the consumer landscape are caused by factors such as the greater availability of electronic data, a greater spectrum of entities and parties involved (e.g. investment banks, servicers), and new laws (e.g. anti-predatory lending laws).

Hot issues on the horizon are municipal litigation, servicing issues and foreclosure defense, assignee liability.

Ms. Bahin discussed regulatory developments. Federal regulators issued revised HOEPA rules this year, possibly to preclude other new legislation intended to regulate the mortgage industry. Generally, the objectives of the new HOEPA rules are to cause lenders to underwrite prudently, permit appraisers to appraise without undue pressure, cause lenders to handle loan payments properly, and to cause lenders to advertise truthfully. These new rules do not address broker compensation, which has been a controversial subject.

Additionally, Congress passed the Housing and Economic Recover Act of 2008, which includes GSE regulatory reform, expands transactions subject to TILA disclosures, establishes the HOPE for Housing program, and mandates mortgage originator licensing.

Ms. Bahin anticipates that Congress will enact legislation in the forseeable future aimed at regulating rating agencies.

Internet Delivery/Electronic Banking
Charles V. Gall, Dreher Langer & Tomkies, L.L.P.

The Internet Delivery/Electronic Banking subcommittee delivered a presentation on the enforceability of online contracts.

Professor Christina L. Kunz of the William Mitchell College of Law discussed proof of assent issues associated with online contracts. Professor Kunz discussed how assent may be obtained in connection with different types of online contracts. For click-through agreements, there is express assent. For browse-wrap agreements, assent may be implied (e.g., use of the website is agreement to the terms).

To have valid assent, there must be (i) adequate notice of the terms, (ii) meaningful opportunity to review the terms, (iii) adequate notice that action is assent and (iv) proof of assent.

With respect to item (i) above, the physical presentation of the terms is important, particularly the placement and format of the terms. For example, assent should not be obtained before notice of the terms is provided.
With respect to item (ii), a consumer's review should not be rushed. In addition, a consumer should be able to navigate forward and backward and not have only one opportunity to review the terms. Rules governing presentation of terms in paper format (e.g., font size requirements, conspicuousness requirements, etc.) should be followed. Hyperlinks can be used to provide access to terms, but pop-up boxes are disfavored as they may be blocked by a consumer's computer.

With respect to item (iii), in order to have express assent, a consumer should have a choice between "yes" and "no."

With respect to item (iv), direct evidence of proof of assent may be maintained by preserving a click stream. Proving acceptance by silence or inaction, however, is not usually valid.

Charles H. Kennedy of Morrison & Foerster, LLP discussed substantive unconscionability issues associated with online contracts. Mr. Kennedy explained that contracts may be deemed unconscionable if, for example, their terms are against public policy or contrary to expectations. Examples of contract terms that have been challenged as unconscionable include:

- Forum selection clauses (presumed valid, but may be defeated by proof of unconscionableness [e.g., too much travel required in relation to the amount in issue]);
- Arbitration clauses (favored and most challenges fail);
- Restrictive licenses (claims of unfair restrictions may be preempted; and
- Limitations of liability clauses.

Mr. Kennedy also discussed issues associated with modification of e-agreements. Such agreements should include a change-in-terms clause. With respect to providing notice of a change, statutory change-in-terms requirements should be followed. Notification by e-mail or otherwise may be sufficient, however, instructing a consumer to check back periodically regarding changes probably is not.

Finally, special problems and issues associated with the enforcement of privacy policies were discussed, including their enforcement by consumer protection authorities such as the Federal Trade Commission and cases in which courts have held that privacy policies are not binding contracts.

Deposit Products and Payments Systems and Truth in Lending
Charles V. Gall, Dreher Langer & Tomkies, L.L.P.

The Deposit Products and Payments Systems and Truth in Lending subcommittee delivered a presentation on proposed changes to Regulations AA, DD and Z.

Sandra F. Braunstein of the Board of Governors of the Federal Reserve System discussed the final rules for the Home Ownership and Equity Protection Act of 1994 ("HOEPA"), which were approved July 14, 2008.

The final rules:

- Change the calculation of the threshold for higher cost mortgages (150 basis points above Freddie Mac index);
• Change HMDA reporting;
• Require underwriting to examine ability to repay for all loans;
• Restrict prepayment penalties (not allowed if payment may change in the first four years); and
• Require escrows.

In addition, (i) for all closed-end mortgages, a servicer must credit payments when received, (ii) creditors and brokers are prohibited from coercing appraisers, (iii) good-faith disclosure of costs must be provided earlier and (iv) unfair and deceptive advertising of mortgage loans is prohibited.

HOEPA rules apply to all creditors and are effective October 1, 2009. The escrow requirements are effective April 1, 2010.

Kathleen Keest of the Center for Responsible Lending commented that overall the rules (e.g., the prepayment penalty restrictions) are a big improvement. She did have some concerns however (e.g., she said that the broker proposal was not sufficient).

Nessa Feddis of the American Bankers Association provided further comments on the rules. She said that there is a concern regarding the definition of a "high-cost loan" and that a manageable index should be used.

Oliver I. Ireland of Morrison & Foerster, LLP discussed the UDAP proposal relating to credit cards that came out in May 2008. Mr. Oliver said that the comment period closed on August 4 and over 56,000 comments had been received. The proposal raises questions on the UDAP authority under the Federal Trade Commission Act. Mr. Oliver further discussed the prohibition against double-cycle billing and the disclosure challenges associated with such a practice.

Ms. Braunstein discussed the June 2007 proposal on credit card disclosures and practices, which spurred more than 5,000 comments. Ms. Braunstein said that the Federal Reserve Board staff is testing the disclosures and that final rules may be issued before the end of 2008. Ms. Braunstein also discussed the proposal regarding the 45-day waiting period for changes in terms and certain advertising issues (e.g., the prohibition against claiming that credit cards have "fixed rates").

Ms. Braunstein also discussed the May 2008 proposal on unfair and deceptive practices issued by the Fed, which would, if enacted in its proposed form:

• Require consumers to have 21 days to make payments;
• Establish allocation of payment requirements;
• Prohibit repricing existing debts except under certain circumstances (e.g., if the borrower is 30 days delinquent or if the card has a variable rate);
• Ban the use of two-cycle billing;
• Cap upfront fees on subprime cards; and
• Prohibit charging overlimit fees because of a hold.

Ms. Feddis addressed concerns with the proposal and explained that UDAP is an unsuitable framework to address credit card and overdraft issues because (i) of its uncertainty, (ii) mainstream practices are labeled unfair and (iii) its potential retroactive effect. Ms. Feddis said that the proposal could lead to a decrease in credit, less innovation, less competition and more costs and that the issues could more appropriately be addressed within Regulation Z.
Ms. Keest discussed significant reforms that she believes are needed in credit card lending, such as restrictions on penalty rates that harm consumers with low incomes. Ms. Keest further discussed access to credit issues, including problematic income-to-debt ratios.

Ms. Braunstein discussed the proposed changes to Regulation DD issued by the Fed, which would require financial institutions to disclose the cost of overdraft programs. Under the proposal, anyone offering overdrafts must give disclosures. Disclosure of available funds at ATMs could not reflect the overdraft amount available, there should also be a right to opt out of having the overdraft paid, and, finally, an overdraft fee would be prohibited if the overdraft was the result of a hold.

Ms. Keest said that overdraft fees are problematic because (i) they are high relative to loan amounts and the time such loans are outstanding, (ii) a small group of people (e.g., people over 55, people dependent on Social Security benefits, minorities) pay the most fees and (iii) overdraft fees may cause a person to go deeper into an overdraft situation. She made several recommendations to improve the proposal, including an opt-in requirement.

Recent Developments in Housing Finance and RESPA
Catherine Andricos, Hudson Cook, LLP

The Housing Finance and RESPA Subcommittee sponsored a session at the ABA Annual Meeting in New York discussing recent developments affecting the mortgage industry. The speakers were Joseph M. Kolar, Buckley Kolar, LLP; Robert M. Jaworski, Reed Smith, LLP; and Mike Flynn, Department of Housing and Urban Development.

Mr. Kolar and Mr. Jaworski focused on the enactment of the Housing and Economic Reform Act of 2008 and its impact on the mortgage industry. Mr. Kolar noted the Act’s higher loan limits, changes to the FHA program and HECM loans, Hope for Homeowners program, S.A.F.E. Act, and new TILA disclosures. Mr. Flynn discussed the impact of the Act's provisions giving HUD $4 billion to disburse to communities, the non-traditional credit rating pilot program, and the servicemember protections.

The panel also discussed the RESPA rule recently proposed by HUD. The proposed rule would require wide-ranging changes to the good faith estimate required by RESPA. Mr. Flynn said that Congress had recently requested that HUD not move forward with the proposed rule. Mr. Flynn also informed the audience that HUD had received more than 11,000 comments on the proposed rule.

Offers of Credit in Debt Collection Communications
Catherine Andricos, Hudson Cook, LLP

The Debt Collection Practices and Bankruptcy Subcommittee sponsored a session at the ABA Annual Meeting in New York on
Ms. Christakis started off the discussion by highlighting potential areas of concern that arise in connection with balance transfer offers for charged-off debt. Ms. Christakis noted that an offer to a debtor to pay a charged-off debt by transferring it to a new credit card might be characterized as a debt collection communication subject to the FDCPA. Mr. Narita provided an overview of litigation addressing this issue in which he has been involved.

Mr. Narita explained that if a debt was previously charged off and is time-barred, a court could find it unconscionable for a party offering to transfer the debt balance to suggest that non-payment of the debt could impair the debtor's credit. See Pettyplace v. Monterey County Bank, Case No. C06-02138 (N.D. Cal.). Where the balance transfer offer is characterized as a debt collection communication, Mr. Narita emphasized the importance of complying with the FDCPA. See Voris v. Resurgent Capital Services, L.P., Case No. 3:06-cv-02253-JM-RBB (S.D. Cal. 2007); see also Hernandez v. Midland Credit Management, Inc., Case No. 04 C 7844 (N.D. Ill.).

Ms. Christakis closed the presentation with a brief discussion of Leckler v. Cashcall, Inc., Case No. C 07-04002 SI (N.D. Cal.). In the Leckler case, the court considered whether, under the TCPA, the debtor had consented, by providing the debt collector with her cellular telephone number, to the debt collector’s use of an autodialer in calling her cellular phone number for collection purposes.

Compliance Management - "Format for Your Compliance Risk Program" - 9:00am-10:00am
Compliance and Operational Risk Management, specifically the Foreign Corrupt Practices Act [FCPA]
Clint Heyworth, Chambliss, Bahner & Stophel, P.C.

Presented by: Compliance Management Subcommittee
Co-Chair: Agnes Bundy Scanlan, Goodwin Proctor, LLP, Boston, MA
Vice Chair: Joanne K Sundheim, JP Morgan Chase, Wilmington, DE
Speakers: Sohayla Fitzpatrick, State Street Global Markets, Boston, MA; Gregory Meredith, JP Morgan Chase, New York, NY

Presentation

Ms. Fitzpatrick initiated the discussion by defining "enterprise risk management" ("ERM"). ERM is an integrated framework for managing credit risk, market risk, operational risk, economic capital, and risk transfer in order to maximize firm value.” Ms. Fitzpatrick stressed that no one part of an organization can control all risks and emphasized a top-down and all-inclusive approach.

Organizations are confronted with various risks from a myriad of different areas. Risk management, internal control programs, SOX program, internal audit, re-engineering initiatives, and compliance confront different business units. Ms. Fitzpatrick stressed multiple frameworks to manage risk can be overwhelming and often do not work. Consequently, the board or senior management should
choose one framework to implement in flexible ways throughout the company.

Operationally, there may be multiple assessment methodologies, overlapping risk evaluation mandates and responsibilities within multiple organizations. Programs should be based on a "framework" of integrated processes, tools and mitigation strategies that assist the organization in managing and measuring operational risk. A cohesive uniform approach across the company that is also individual enough to manage individual risks with different business units in a company is necessary. According to Ms. Fitzpatrick, operational risk management is more art than science.

Ms. Fitzpatrick said that the operational risk management structure at State Street is a matter of culture training and governance. The program is ongoing. Identification, assessment and training are key. The framework supports management in aligning business and risk management goals and optimizes risk/reward decisions. The framework drives the strategy and value proposition. It also engages management in active management of risk. The ERM provides foundational structure enabling consistency and best practices across the organization. The ERM also articulates the approach and the sound practices. Finally, the ERM demonstrates effective operational risk management to interested parties (e.g. regulators, auditors, clients, shareholder and rating agencies).

The program value proposition should be communicated to the businesses. The ERM must incorporate strategy, business value, the shared vision, mature methodologies, priorities beyond compliance, how to leverage all programs cohesively and how all this supports profitable growth.

Companies should consider programs that provide timely information to the board so that the board can continue to manage from the top down. Keys to strong management include: governance, reporting, business environment internal control, external loss events, scenario analysis and risk assessment. Key managers should be intimately involved with developing the procedures so that the risk manager is never made the scapegoat when something goes wrong, and so that the managers are empowered to better manage their own risks.

Engaged senior management and boards of directors are necessary and should establish clear policies and communicate their appetite for risk. Specific procedures for today: strengthen the culture top to bottom, encourage transparency, follow up on warning signs, establish common terms across organizations with global presence, create standard deep-dive internal control criteria, create a control library to leverage control design and investment, and analyze data for trends to anticipate upcoming issues. Be proactive not reactive. Ultimately, diligence in risk management saves the company, shareholders and society money.

**Foreign Corrupt Practices Act**

Mr. Meredith provided a brief overview of the FCPA, 15 U.S.C. §§ 78dd-1, et seq. Essentially, the statute covers issuers, domestic concerns, and non-U.S. persons, but ultimately, the DOJ uses this act to broadly cover U.S. and non-U.S. entities. The act is divided into two sections. The first section is the anti-bribery section. The second addresses the record keeping provisions mandating accurate reporting and reasonable controls. Globally,
many treaties and international statutes conform to the FCPA.

Mr. Meredith described the FCPA as a statute that prohibits and makes it a civil and criminal offense for anyone subject to U.S. jurisdiction to offer, promise, give or authorize the giving of anything of value to a non U.S. official, directly or indirectly to secure an improper business advantage. The jurisdictional hook is using the mail or any means or instrumentality of interstate (or foreign) commerce to violate the law. Mr. Meredith emphasized "anyone" means a company or individual or any individual acting for a company. A non U.S official is any government employee or state controlled company. Further, political parties and even consultants may fall under the definition of non-U.S. person.

Companies should understand these definitions and standards so that they can develop procedures that will demonstrate the company actively sought to encourage proper behavior. Various prohibited practices exist and companies should be familiar with them.

The FCPA exempts "grease payments" from the prohibition. "Grease payments" are payments made to to expedite or secure performance of a routine governmental action by a foreign official or political party. The term is defined to mean only an action which is ordinarily and commonly performed by a foreign official. Two defenses exist: legal actions in another country and certain expenditures for reasonable expenses. Mr. Meredith emphasized the detailed nature of these defenses.

Companies should develop procedures to identify red flags involving travel, lodging and entertainment. Companies should identify proper procedures and specific methods for recording expenses properly. Companies should also identify types of employee transactions that may involve improper procedures on behalf of an employee. Mr. Meredith emphasized due diligence processes for international consultants, business development consultants and portfolio companies.

Can Privacy and Marketing Co-exist? Don't Ask - Don't Sell
Clint Heyworth, Chambliss, Bahner & Stophel, P.C.

Presented by: Personal Property Financing Subcommittee
Co-Chair: Thomas J. Buiteweg, Hudson Cook, LLP
Co-Chair: Mark S. Edelman, McGlinchey Stafford, PLLC
Vice Chair: Robert A. Aitken, Ford Motor Company

Presentation

The Personal Property financing subcommittee session addressed whether privacy and marketing can co-exist. Thomas J. Buiteweg and Mark S. Edelman led the discussion. The panelists included Steven VanMeter from the OCC, L. Richard Fisher from Morrison and Forester, and Allen Hile of the FTC.

Financial Privacy Overview - Stephen VanMeter

Mr. VanMeter briefly reviewed relevant federal laws. He noted that
the Gramm-Leach Bliley Act, ("GLBA") and Fair Credit Reporting Act ("FCRA") both have provisions related to privacy. The main idea, according to Mr. VanMeter, is that companies must tell consumers they are going to share information before they actually do so. Companies must give consumers the opportunity to opt out—and companies must honor opt-outs.

Mr. VanMeter suggested the laws differ as to the substance of the opt-out in scope, definitions, exceptions, applicable entities and penalties. The FCRA applies to "persons", but have a tie to financial institutions. By contrast Mr. VanMeter said the GLBA only applies to financial institutions which is broadly defined.

Mr. VanMeter emphasized that FCRA has civil penalties, but that GLBA can be enforced only by designated administrative agencies. The type of information covered by the two laws also differs. GLBA covers all non-public personal information, whereas FCRA applies only to information that meets the statute's definition of "consumer report."

According to Mr. VanMeter, Short Form Privacy Notices, Firm Offers of Credit and Affiliate Marketing Rules are all current hot topics.

L. Richard Fischer

Mr. Fischer emphasized, that the GLBA is a "sharing rule" and the affiliate marketing rule is a "use rule." The affiliate marketing rule does not regulate when information can be shared with an affiliate, but does regulate when the affiliate may use the information for marketing.

A company may avoid these rules under very specific circumstances, for example if the company prevents disclosing information to other parties.

Mr. Fischer emphasized the "existing customer" exception under the affiliate marketing rule. Finally, if a company can use "depersonalized" information, the company will not trigger these rules.

Federal Trade Commission -- Allen Hile

Mr. Hile said that the statute requiring the establishment of the "Do Not Call" registry is probably the most popular federal statute ever. Sellers must pay to access the registry and then must follow the limitations applicable to such registry. Companies may call any consumer with whom they have an established relationship within 18 months. Companies may also communicate with consumers who give them permission. Consumers may also opt out with a specific entity. Calls on behalf of non profit companies for fund raising do not need to comply. However, such non profits must follow a specific entity do not call list maintained internally. Several states also maintain "do not call statutes."

The CAN SPAM Act governs e-mail advertising. Companies must maintain an internet-based opt-out notice. Any opt-out by a consumer must be honored within ten days of its transmission. Under the Act, the Consumer only needs to send an email to exercise the opt out.

Mr. Hile related the FTC's inquiry into online behavioral advertising. This type of advertising is based on a consumer's online habits. The FTC's research indicates some benefits to the consumer by reducing and making more advertising specific to
Committee Forum: Regulatory Issues Impacting Reverse Mortgages

Emily G. Miller, Hudson Cook, LLP

The Consumer Financial Services Committee presented a Committee Forum on Reverse Mortgages. The panelists were Jim Milano and Joel Schiffman of Weiner Brodsky Sidman Kider PC; Nina Simon of the AARP Foundation; and Arthur Axelson of Reed Smith.

Mr. Milano began the presentation with a breakdown of the aging US population and explaining that reverse mortgages appeal to those whose net worth is mainly tied up in their home equity. Over 22 million households are headed by individuals that are 65 or older. 70% of elderly owned homes are owned free and clear. Traditionally, the decision to get a reverse mortgage is a lifetime decision, usually prompted by a negative event, such as deteriorating health, death of a spouse, or overdue taxes. The typical reverse mortgage applicant was a 70 year old or older widow who was "house rich and cash poor." Today those demographics are changing. More seniors are taking out reverse mortgages to refurbish their home and make them more "senior-friendly." Some use reverse mortgage proceeds to travel, pay for their children or grandchildren to get an education, or for various recreational expenses.

The Truth in Lending Act provides the definition of "reverse mortgage" for federal disclosure requirements. The FHA provides standards for being insurable. Currently the FHA insures Home Equity Conversion Mortgages or "HECMs." All HECMs are reverse mortgages, but not all reverse mortgages are HECMs. During the credit boom a few years back, more private industry lenders were offering their own types of reverse mortgages. However, in today's market, the proprietary types have decreased and most reverse mortgages originated are HECMs.

Mr. Schiffman presented an over view of the original legislation and FHA guidance that provided for reverse mortgages and the new federal HERA legislation's impact on the HECM program. The three primary sources for reverse mortgage authority is Part 206 of title 24 of the Code of Federal Regulations, the HUD HECM handbook (and other reverse mortgage related HUD handbooks), and HUD Mortgagee letters.

Some of the changes to the HECM program include the following:

- HECMs will be allowed in connection with co-ops.
- HECMs can be made for home purchases.
- There will be a higher FHA loan limit.
- Lenders can no longer be involved with the funding of HECM counseling.
- The origination fee will be reduced - 2% of the first $200,000, 1% for anything over $200,000, subject to a maximum of $600. The broker fee must come out of the origination fee.
- Mortgagors that participate in the HECM program cannot participate in any other financial services (but you can set...
Ms. Simon then presented information demonstrating the cost and recent popularity of reverse mortgages and discussed study findings by the AARP. The AARP conducted a reverse mortgage study that included contacting applicants for reverse mortgages and asking them questions related to the loan process and the purposes of the mortgage. The study found that most recipients used the money to pay off debt. Over half of the applicants obtained the reverse mortgage; over two-thirds of those that decided not to obtain a reverse mortgage cited the high cost as the reason.

Ms. Simon said that cost is the single biggest impediment to consumer acceptance of reverse mortgages. Some upfront costs can be as high as a $14,000 - $15,000 origination fee, a $6,000 mortgage insurance premium, and $2,000 - $3,000 in closing costs. Ms. Simon concluded that more research is needed. These studies are short term studies and do not reveal the long term impact of reverse mortgages on the financial well being of borrowers. Ms. Simon provided some recommendations on how to make the product more consumer-friendly, including reducing the origination fee cap, lowering mortgage insurance premiums, and removing the FHA loan limit.

Ms. Simon also discussed recent scams involving reverse mortgages. In Atlanta, investors are getting seniors to rent a property, after which the investor puts the senior's name on the title for a cheap foreclosure sale and then requires the senior to get a HECM to pay off the investor. Further investigation is warranted if a title search shows a foreclosure and the HECM is in a different person's name than who was on the title at foreclosure.

Mr. Axelsson discussed how various existing federal laws apply to HECMs. HECMs are HMDA-reportable loans. Reverse mortgages are within the definition of federally related mortgage loans and as a result, Section 8 of RESPA applies. The RESPA broker rules apply. The HUD-1 requirement applies and the TILA disclosure requirements apply. You have to make certain assumptions about the mortgage to determine which disclosures must be given. The appropriate disclosures must be given and the reverse mortgage must meet the TILA definition. If it doesn't comply it might be subject to HOEPA and you can not have that because HOEPA prohibits negative amortization. If the product is open-end, the TILA HELOC disclosures are required.

Mr. Axelsson also warned lenders to not forget about state law requirements and HECM disclosure requirements established by HUD.

Fair Access to Services Subcommittee

*Emily G. Miller, Hudson Cook, LLP*

The Fair Access to Services Subcommittee presented recent developments in fair access to credit. The panelists were Heather Thayer of Wells Fargo and Any Salberg of Whyte Hirschboeck Dudek, S.C.

Ms. Salberg discussed a bill in the House of Representatives that would establish a "bill of rights" for credit card holders. The bill
would prohibit universal default clauses, minimize arbitrarily-increased rates, and cap over limit fees. The bill is not expected to pass this year.

Ms. Thayer discussed how lenders can determine when fraud has been a factor in the origination of a HELOC and when a lender can terminate, restrict, or reduce the HELOC due to that fraud. A lender might be permitted to terminate a HELOC if, for example, the borrower represented to the lender that the home would be owner-occupied when it was in fact an investment property. The lender must determine whether it was the borrower or the broker that represented that the property was owner-occupied. If the borrower made the representation, then the lender generally may close the HELOC.

Ms. Thayer also discussed a new issue facing lenders relating to line management. Lenders would like to restrict lines before they go into default. TILA allows "temporary reductions" when there is a material adverse change in the borrower's financial condition and as a result the creditor believes the borrower will be unable to pay. TILA also allows "temporary reductions" when there is a substantial reduction of at least 50% of the equity cushion. The problem is calculating 50% of 0 when 100% of the property was financed. Another problem with these reductions is that the credit reporting agencies do not have a code for these transactions, so a reduction on a credit limit makes it appear as though the borrower has less credit available and it has a negative impact on the borrower's score. However, if the lender just restricts the line altogether it doesn't affect the borrower's score.

Another new issue lenders are facing is that when a borrower passes away, the family may use the borrower's line to pay for funeral and estate expenses.