

Memorandum



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DATE January 31, 2008

TO Lenders Making Residential Mortgage Loans in Massachusetts

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RE Limitations on Subprime Loans to First Time Home Loan Borrowers

A new Massachusetts statute governing subprime loans to first time home loan borrowers became effective today (January 31, 2008) and the Division of Banks released a Regulatory Bulletin (#1.3-104) implementing the new statute yesterday. Although the Regulatory Bulletin is effective immediately, the Division of Banks will accept comments on it until February 20, 2008.

The new statute, Massachusetts General Laws ch. 184 § 17B½, prohibits making a subprime adjustable rate mortgage loan to a first time home loan borrower unless (a) the borrower completes counseling regarding the advisability of the loan transaction with an independent counselor prior to closing; and (b) the borrower “opts in” to the transaction in writing after completing counseling.¹

¹ Massachusetts General Laws ch. 184 §17B½, which was enacted as Section 7 of Chapter 206 of the Acts of 2007 on November 29, 2007 and is effective January 31, 2008, provides as follows:

No mortgagee who makes a loan to a first-time home loan borrower, to be secured by a mortgage on owner-occupied, 1 to 4 family residential property in the commonwealth, shall make a subprime loan at a variable or adjustable rate of interest unless the mortgagor affirmatively opts in writing for the variable or adjustable rate subprime loan and receives certification from a counselor with a third-party nonprofit organization that the mortgagor has received counseling in person on the advisability of the loan transaction; provided, further that said third party nonprofit organization shall have been approved by: (1) the United States Department of Housing and Urban Development; (2) a housing financing agency of the commonwealth; (3) the Massachusetts Homeownership Collaborative; (4) or the regulatory agency which has jurisdiction over the mortgagee. The commissioner of the division of banks shall maintain a list of approved counseling programs. At or before closing such a loan, the mortgagee shall obtain evidence that the mortgagor has completed an approved counseling program. If such subprime mortgage loan is made by a mortgagee in violation of this section, the variable or adjustable rate terms of the loan shall not be enforceable and the mortgagee shall only be entitled to collect an interest rate equal to the lesser of the original interest rate, including any discounted rate, or the current adjusted interest rate throughout the remaining term of the loan. The commissioner of banks shall issue directives or guidelines or adopt regulations to administer and carry out this section and to further define the terms used in this section.



Regulatory Bulletin 1.3-104² contains definitions of the terms used in §17B½.

“First time home loan borrower” is defined as “a natural person obtaining a mortgage loan to purchase a residential property for the first time.”

“Mortgage Loan” is defined as “a loan to a natural person made primarily for personal, family or household purposes secured wholly or partially by a mortgage on residential property.”

“Residential Property” is defined as real property located in the commonwealth improved with a 1- to 4-family dwelling, occupied or to be occupied, in whole or in part by the obligor on the mortgage loan, but excluding vacation homes and investment properties.

A “Subprime Loan” is defined as:

For first-lien transactions, a transaction in which:

- a. the loan amount falls within the loan amount limits set forth by the Federal National Mortgage Association (“FNMA”) or the Federal Home Loan Mortgage Corporation (“FHLMC”), but the loan fails to meet the federal agencies’ underwriting guidelines; or
- b. the loan amount exceeds the loan limits set forth by FNMA and FHLMC and the annual percentage rate (APR)³ is greater than **two and one-half (2.5)** percentage points above the yield on United States Treasury securities having comparable periods of maturity, as of the 15th day of the month immediately preceding the month in which the application for the extension of credit is received by the creditor.

For “simultaneous second lien” transactions⁴, a transaction in which:

the APR for the simultaneous second lien is greater than **five (5.0)** percentage points above the yield on United States Treasury securities having comparable periods of maturity, as of the 15th day of the month immediately preceding the month in which the application for the extension of credit is received by the creditor.

If a loan falls within this definition of “subprime,” is made to a “first time home loan borrower,” and provides for a variable rate of interest, the lender must obtain, prior to closing (a) written certification from a counseling agency approved by the Division⁵ that the borrower received

² The full text of Regulatory Bulletin 1.3-104 can be found on the Division of Banks’ website. Go to www.mass.gov/dob, and click on “Laws and Regulations” in the “Legal Resources” section at the bottom of the home page.

³ The APR is to be computed in accordance with truth in lending laws.

⁴ A “simultaneous second lien” transaction is defined as “a loan secured by a second or subsequent mortgage lien originated and closed in conjunction with a first mortgage loan on the same residential property, the proceeds of which are used as part of the purchase price of the residential property.”

⁵ A list of approved counseling agencies can be found on the website of the Office of Consumer Affairs and Business Regulation. Go to www.mass.gov/ocabr and click on the “consumer” tab or search for “counseling agencies” by using the search feature in the top right corner of the home page.



counseling in person on the advisability of the loan transaction; and (b) a separate written statement from the borrower affirmatively opting in to the adjustable rate subprime loan. The opt-in statement must be printed in at least 16-point capitalized boldface type and may be signed only after the borrower has completed counseling.

If a lender makes a subprime loan to a first time home loan borrower without satisfying these conditions, the adjustable rate provision will not be enforceable and the rate at which the lender may collect interest over the term of the loan is limited to the lesser of (a) the original interest rate, including any discount; or (b) the current adjusted interest rate.⁶

The Division of Banks published no additional guidance with the Regulatory Bulletin. If you have questions or concerns, please call me (at 617-856-8343) or send me an email (at NWilsker@brownrudnick.com). To the extent I don't have answers to your questions, we may wish to consider submitting comments to the Division of Banks prior to the February 20th deadline.

⁶ It is unclear what the "current adjusted interest rate" would be if not the initial rate, since a loan made in violation of the statute would be subject to the fixed rate requirement from the date of inception.