

Lexington Lending
Mortgage Compliance Guide
For
Brokers

Mortgage Compliance for Brokers

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I. Mortgage Industry Compliance

Over the years, numerous laws have been enacted by Congress to protect the consumer and prevent discrimination during and after the process of obtaining a mortgage. As such it is vitally important that all lenders participating in the lending of federally related mortgage loans, whether you are involved in the retail or wholesale lending of such loans be familiar with the laws that govern our industry. In many cases non-compliance with these laws and regulations may carry severe penalties and can result in costly liability suits and criminal prosecution for the parties involved as well as class action lawsuits that effect the industry as a whole.

Lexington requests that all of our Wholesale customers including underwriters, originators, and processors be familiar with the impact and importance of these laws in their area of responsibility. The Wholesale Broker Agreement and this Compliance Manual require that all loans offered for sale are in full compliance with all applicable federal, state and local statutes and regulations. State and local laws and regulations may apply depending on your location.

CAUTION: These laws are extremely complex, very detailed and frequently amended. Accordingly, Lexington does not warrant the accuracy of the information provided concerning these laws and regulations. These guidelines are not in any way a substitute for the Wholesale Broker own compliance procedures. You are urged to consult with an attorney should you have any compliance questions.

II. Real Estate Settlement Procedures Act –(RESPA)—Regulation X Introduction to RESPA

The Real Estate Settlement Procedures Act (RESPA)- also known as Regulation X was first enacted in 1974. The law was enacted to affect changes in the settlement process for residential real estate that would result in more effective disclosure to both homebuyers and sellers of the settlement costs associated with the transaction. The law also provides guidelines as to what fees and charges are not permissible by defining illegal kickbacks or referral fees that unnecessarily increase the cost of settlement services as well as reducing the amounts that homebuyers are required to place in escrow accounts.

Lexington Lending requires that all loans purchased from our customers be in compliance with the Real Estate Settlement Procedures Act (RESPA). As such it is necessary to inform and educate our customers as to the correct procedures to be followed in order to remain in compliance with the law.

The following is a broad overview of the key factors to be considered under RESPA:

Illegal Kickbacks-Section 8(a)

To protect consumers from unscrupulous lending practices where kickbacks and unearned fees are paid by or to lenders and other entities involved in the loan process, Section 8 of RESPA was passed.

Section 8(a) of RESPA prohibits the illegal use of kickbacks and unearned fees in a mortgage transaction. These kickbacks can be received by anyone involved or "incident to" the loan process including the lender, or any other applicable third party such as appraisers, flood vendors, etc. In this vein RESPA mandates that all fees be correctly disclosed on the HUD-1.

Fee-Splitting- Section 8(b)

The Department of Housing and Urban Development (HUD), continues to uphold its interpretation of Section 8(b) of RESPA. This Section indicates that any up-charge (charging fees above what is actually earned by a service provider), regardless of whether that overcharge is split with another entity associated with the transaction, constitutes a violation of RESPA. Fees, which are paid to third parties, need to clearly be noted as P.O.C. (Paid Outside of Closing) items on the HUD-1, and the name of the service provider must be disclosed

WARNING: HUD has made clear that it takes Section 8 of RESPA very seriously and pursues any allegations of violation of this section aggressively.

Correct Disclosure of Fees Paid to Lender

It is important that all fees are accurately disclosed on the HUD-1 Settlement Statement at closing. In certain circumstances some fees issued by the lender may from time to time be subject to a fee reducing credit. An example of this may be Lexington Lending issuing a credit for utilizing certain underwriting services when registering or locking loans. This credit will reduce the typical Administrative Fee charged by Lexington. As such, that reduced fee should be disclosed on the HUD-1 instead of the fee that would normally be charged. For clarification, see the example below.

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*Example:

A broker is issued a \$100 credit. The Administrative Fee charged by Lexington is typically \$1250. On the final HUD-1, the Administrative Fee should be listed as \$1150 in this example.

809. Administrative Fee paid to Lexington Lending FSB \$1250.00.
810. Tax Service Fee paid to XYZ Title Co. by Lexington Lending (\$72.00 P.O.C.)
811. Flood Cert. Fee paid to XYZ Flood Co. by Lexington Lending (\$12.00 P.O.C.)

Good Faith Estimate

RESPA mandates that the lender must provide a Good Faith Estimate of Settlement Services and their associated costs to the consumer to facilitate understanding, prior to settlement, of the costs associated with the loan for which they have applied. The following are key points to remember regarding the GFE:

- The GFE must be disclosed within 72 hours of a new mortgage application.
- The GFE must disclose the providers of settlement services whenever possible. Settlement services include fees for underwriting, processing, origination, etc.
- The yield-spread premium must be disclosed on the GFE or at least estimated for loans that are not yet locked.

Fees disclosed on the initial GFE should always closely approximate the actual fees shown on the HUD-1. Any large discrepancies in these fees will raise red flags and can create potential liabilities for the lender involved.

Servicing Disclosure Statement

At the time of application for a mortgage loan, or within (3) three business days thereafter, the lender or broker who anticipates using table funding, must provide the borrower a Servicing Disclosure Statement. This disclosure indicates to the consumer the possibilities of his or her loan being transferred to another entity for servicing.

The following guidelines should be adhered to with regard to the Servicing Disclosure Statement:

1. For loans closing in the broker's name: only one servicing disclosure statement is required which contains information specific to that individual broker.
2. For loans closing in Lexington 's name: the broker's Servicing Disclosure from (1) above is required in addition to a second Servicing Disclosure completed with Lexington 's information. This disclosure should be completed as follows:

Under Servicing Transfer Estimates:

- Question #1 should indicate that Lexington: "may assign, sell or transfer the servicing of your loan while the loan is outstanding"
- Question #2 should have the selection checked which states "76-100%" for percentage of loans which will have servicing rights transferred.

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- Question #3 should have checked the statement that reads " We have previously assigned, sold or transferred the servicing of federally related mortgage loans."

Note: Loans that are closing in Lexington's name must have (2) disclosures submitted in the final closed file. These are the broker's Servicing Disclosure Statement which discloses information pertinent to the broker as well as the servicing disclosure with Lexington's information as outlined above.

Uniform Settlement Statement (Form HUD-1)

RESPA mandates the use of a standard settlement form or Uniform Settlement Statement (HUD-1) to be used in all mortgage loan closings to identify and codify the cost of the credit extended. RESPA also specifies the terminology, sequence, and numbering on certain sections of the HUD-1 and stipulates which sections are required. Lenders are allowed to print or reproduce their own HUD-1 forms as long as they contain the required information.

The HUD – 1 should closely approximate the charges disclosed on the initial Good Faith Estimate. There should be no large discrepancies between the HUD-1 and the initial Good Faith Estimate.

Fees, which are paid to third parties, need to clearly be noted as P.O.C. (Paid Outside of Closing) items on the HUD-1, and the name of the service provider must be disclosed.

Disclosure of Yield Spread Premiums

Any Yield Spread Premiums paid to a Broker must be accurately disclosed on the HUD-1. The requirements for disclosure of Yield Spread Premiums are as follows:

- Any "funded" loan closed with the lender's (Lexington's) funds must have the yield spread premium disclosed to the borrower on the Good Faith Estimate **and** on the HUD-1.
- This disclosure must take place on the "800" series on the GFE and HUD-1.
- The disclosure must state the amount of the Yield Spread Premium, who it was received by and who it was paid by.

Example:

809. Yield Spread Premium to XYZ Mortgage paid by Lexington \$2,500 P.O.C. (Paid Outside of Closing).

Escrow Accounts

An amendment to RESPA was passed in 1994, which changed the accounting method used to calculate the amounts held in borrowers' escrow accounts. This change was meant to benefit the consumer by reducing the amount of a borrower's funds that the lender could hold in an escrow/impound account. Lenders are required under this revision to itemize individual escrow deposits on the 1000 series of the HUD-1 using single line-item accounting, and also to show an adjustment based on aggregate accounting. This adjustment will equal the difference in the deposit required under aggregate accounting and the sum of the deposits under single-item accounting.

RESPA establishes requirements for escrow accounts that are established in connection with

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federally related mortgage loans. An escrow account is any account that a Servicer establishes or controls on behalf of a borrower to pay taxes, insurance premiums (including flood insurance), or other charges with respect to the loan. As stated above RESPA sets limits for the amount of money a lender can hold in an escrow account using calculations based on monthly payments and disbursements within a calendar year, limits the amount of cushion a lender can use, and how overages and shortages in the account are handled.

Aggregate Accounting Method- Under the aggregate accounting method, all elements of an escrow account are considered as a single annual sum when computing the amount for the initial and monthly escrow deposits necessary to meet yearly expenses of all escrowed items.

RESPA also mandates that the lender must conduct an escrow analysis to determine the amount the borrower needs to deposit into the escrow account and the amount of the borrowers periodic payments will be, using the aggregate accounting method. This analysis must be provided to the borrower at closing or within 45 days of the establishment of the escrow account.

II. Truth In Lending Act – (TILA) -- Regulation Z

Congress established the Truth in Lending Act in 1969 to establish regulations on the amount and type of credit information disclosed to the consumer. This act is implemented by the Federal Reserve Board under Regulation Z. The terms "Truth in Lending" and "Regulation Z" are often used interchangeably and both the act and the regulation have been amended several times over the years.

The TILA (Reg. Z) establishes model disclosure forms which lenders may use as guides to creating the disclosures they provide to their borrowers. These model forms facilitate lender compliance with the act and aid the consumer in understanding the costs of the credit transaction.

Under TILA, mortgage bankers are required to disclose to the borrower, the terms and cost of the credit they are receiving before the applicant becomes contractually liable of the loan at settlement.

Truth in Lending Disclosure

The Truth in Lending Disclosure displays the terms and cost associated with the mortgage loan.

This disclosure contains a total of 14 individual items which must be disclosed, five of which are "material disclosures" which must be displayed in a particular way to allow consumers ease of comparison.

1. **Annual Percentage Rate (APR)** is the cost of credit expressed as a yearly rate. The APR can be calculated by using the actuarial methods described in Appendix J of Regulation Z. If the APR changes by more than the stated tolerance between the delivery of the early required disclosures and consummation, the lender must either provide a complete set of new disclosures or provide the changed terms to the borrower by consummation or settlement, whichever is later.
2. **Finance Charge.** The Finance Charge is the cost of credit expressed as a dollar amount. It includes any charge payable directly or indirectly by the applicant and imposed directly or indirectly by the lender as a condition of receiving credit.

The finance charge includes but is not limited to the following types of charges:

<ul style="list-style-type: none">• Loan Origination Fee• Loan Discount Fee• Loan Commitment Fee• Borrower paid Mortgage Broker Fees• Inspection Fee• Processing Fees• Underwriting Fee• Tax Service Fee• Flood Certification Fee• Escrow/Impound Waiver Fee• Assumption Fee	<ul style="list-style-type: none">• Interest• Courier Fees• Mortgage Insurance Premiums• Service, transaction, activity and carrying charges• Loan Fees, Finders Fees and similar charges• Premiums for credit life, accident, health or loss of-income insurance, written in connection with a credit transaction• Document Preparation Fee• Closing Fees, including Attorney's fees
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Examples of fees **not** included in the Finance Charge:

• Points and Fees paid by the Seller
• Application fees charged to all applicants for credit
• Fees for preparing deeds or mortgages
• Fees for title examination, abstract of title, property survey
• Amounts required to be paid in escrow or trustee accounts
• Notary or appraisal fees
• Any escrowed fee or money on reserve for taxes and insurance
• Recording Fees
• Well and Septic inspection fee
• Final inspection fee
• Termite inspection
• Flood Hazard inspection

3. **Amount Financed.** The “amount financed” is the amount of credit provided to the borrower or on their behalf and is calculated by:

- Determining the principal loan amount (subtracting any down payment).
- Adding any other amounts that are financed by the lender and are not part of the finance charge.
- Subtracting any prepaid finance charge.

4. **Total of Payments.** The “total of payments” means the total amount the borrower will have paid when they have made all scheduled payments.

5. **Schedule of Payments.** The schedule of payments includes the dollar amount and timing of payments scheduled to amortize the loan, excluding any down payment. The dollar amount of payments must include all components of the finance charge, including mortgage insurance escrows.

Right of Rescission

TILA mandates that for any mortgage loan transaction involving the transfer of security interest of the borrowers principle dwelling (a refinance or equity loan), each consumer who has an ownership interest in the financed property, has a right to rescind the transaction, without penalty, by midnight of the third business day following consummation of the loan.

If a loan transaction is subject to the right of rescission, a lender must deliver two copies of the right to rescind notice to each of the consumers who has the right to rescind. The lender may not disburse any loan proceeds other than into escrow, perform any services or deliver any materials until the rescission period has expired and the lender is reasonably satisfied that the applicant has not rescinded.

Section 32-Predatory Lending

As the result of largely anecdotal evidence that predatory lending practices were on the rise, Congress began to pay more attention to these practices and recognized the need to pass legislation that would curb these practices. Though most forms of predatory lending occur in the sub-prime mortgage market, Congress felt the need to protect consumers from those lenders that were engaging in certain practices that could be defined as predatory in nature. Among these practices are:

- Equity Lending- Making unaffordable loans based solely on a borrowers equity and not on the borrowers ability to repay the loan.
- Loan Flipping- Providing inducements for a borrower to refinance a loan repeatedly, even though the refinancing may not be in the borrower's best interest, and charging points and fees for each refinance. Also known as "equity stripping".
- Loan Packing- Including unnecessary insurance in the loan obligation and fraudulently concealing the insurance from the borrower.

As a result of these kinds of practices, Congress passed HOEPA (Homeowners Equity Protection Act) to amend TILA in 1994. HOEPA identifies predatory loans through the use of rate and fee triggers and provides consumers entering into these transactions with special protections. A loan is covered by HOEPA if one of the following thresholds are met:

1. the APR exceeds the rate for Treasury Securities with a comparable maturity by more than eight (8) percentage points (revised in 2001) or;
2. the points and fees paid by the consumer exceed the greater of eight (8) percent of the loan amount or \$480 (revised 2001), adjusted annually based on the Consumer Price Index (CPI).

Creditors offering HOEPA-covered loans must give consumers an abbreviated disclosure statement at least three business days before the loan is closed in addition to the disclosures mandated by TILA at or prior to closing. HOEPA also restricts certain loan terms for high cost loans because they are associated with abusive lending practices. These terms include short-term balloon notes, prepayment penalties, non-amortizing payment schedules and higher interest rates upon default.

Note: Lexington Lending does not purchase or fund loans covered by HOEPA or any state predatory lending law.

III. Equal Credit Opportunity Act—(ECOA) -- Regulation B

To prevent discrimination of the borrower in a loan transaction, The Equal Credit Opportunity Act was passed along with its implementing regulation –Reg. B, in 1975. ECOA is based on the need to ensure that financial institutions throughout the United States engage in the extension of credit without discrimination on a defined basis.

The Act provides protection against discrimination under the seven prohibited bases below:

- Sex
- Marital Status
- Age
- Color
- Race
- Religion
- National Origin

ECOA sets forth certain practices and acts, which lenders are permitted in taking, evaluating, and acting on the application for credit. It also mandates guidelines for furnishing and maintaining credit information. In addition, ECOA provides guidelines that regulate the following:

- Information gathering and dissemination
- Investigation requirements
- Standards of Creditworthiness
- Terms of Credit
- Furnishing of Credit Information
- Revocation, alteration or termination of credit
- Loan collection procedures

Notifications

ECOA also mandates the use of a model disclosure that informs the borrower that the lender may not discriminate against them based on the above listed criteria. Other notifications are also mandated, among which are the following:

- Notification that the creditor has approved credit.
- Notification of Counter Offer- If a lender cannot grant credit under the original terms applied for but is willing to offer a loan under different terms.
- Notice that the creditor did not approve the application request, and the reasons for the denial

Rules for Providing Appraisal Reports

A creditor that provides appraisal reports only upon request must notify an applicant in writing of the right to receive a copy of an appraisal report. The notice may be given at any time during the application process but no later than when the creditor provides notice of action taken. A creditor must mail or deliver a copy of the appraisal report within 30 days after the creditor receives an applicant's request, receives the report, or receives reimbursement from the applicant for the report, whichever is the last to occur.

Compliance

ECOA is implemented by the Federal Reserve Board of Governors. Failure to comply with ECOA can result in any or all of the following liabilities:

- All actual damages sustained by the applicant,
- All costs of the action, including court costs and reasonable attorney's fees,
- Punitive damages in an amount not to exceed \$10,000 for an individual action.

ECOA is enforced under Section 8 of the Federal Deposit Insurance Act and enforced by twelve different Federal Agencies including: Office of the Comptroller of the Currency (OCC), the Federal Reserve Board (FRB), Office of Thrift Supervision (OTS), Federal Deposit Insurance Corporation (FDIC) and the National Credit Union Administration (NCUA). These agencies enforce ECOA by conducting compliance examinations of the various financial institutions within their jurisdictions.

IV. Fair Credit Reporting Act

The Fair Credit Reporting Act was passed into law as part of the Consumer Protection Act in 1968. FCRA is designed to assure that consumer-reporting agencies exercise fairness, confidentiality, and accuracy in preparing and disclosing credit information. It limits the furnishing of credit reports to those authorized to receive them, and it places disclosure obligations on the users of consumer credit reports. The Act also permits consumers to obtain credit information about themselves from Credit Bureaus and to dispute inaccurate or incomplete information.

As all mortgage companies use credit reports in evaluating a consumer's application, they are subject to some of the requirements of the FCRA. The Act specifically defines the permissible purposes for access to a consumer's credit file:

- Credit or insurance analysis purposes
- Employment Purposes
- Court Order
- Written instructions of the Consumer
- To determine eligibility for some license or other benefits granted by a governmental agency.
- Legitimate business need for information in connection with a business transaction.

Establishment of Time Limits on Obsolete Information

The Act also regulates the time limits for which certain information must be deleted from the credit report files. The following are limits for various areas of credit information:

- Bankruptcy Information cannot be kept longer than ten years from the date of entry of the order for relief or the date of adjudication.
- Suits and judgments cannot be kept longer than seven years from the date of payment, or until
- the governing statute of limitations has expired, whichever is longer.
- Paid tax liens cannot be kept longer than seven years from the date of payment or until the
- governing statute of limitations has expired, which ever is longer.
- Accounts that were placed in collection or charged-off losses cannot be kept longer than seven years.
- Criminal or related records from the date of disposition, release, or parole cannot be kept longer than seven years.
- Any other adverse item cannot be kept longer than seven years.

Whenever information on a consumer credit report causes the lending institution to decline or adversely affect the credit request, the lender must notify the consumer of the name and address of the consumer reporting agency making the report.

Disclosures

The FCRA mandates disclosure by the user of a credit report to the borrower if there is either a denial of credit or an increase in the cost of credit based on information obtained in the credit file. The credit repository used in the decision must also be revealed in this disclosure, and copies of the disclosure statement must be retained by the issuer of credit for two (2) years.

Enforcement

Primarily the Federal Trade Commission enforces the Fair Credit Reporting Act. The FCRA provides criminal penalties for users if information is obtained from a credit report under false pretenses and for credit bureaus if credit information is provided to anyone unauthorized to receive it. In addition to criminal prosecution, consumers may bring civil suit for actual and punitive damages against credit bureaus or users of credit reports for either willful or negligent noncompliance with the act.

V. Flood Disaster Protection Act

The Flood Disaster Protection Act (FDPA) was passed by Congress in 1973 to expand the National Flood Insurance Program established by the National Flood Insurance Act of 1968. The purpose of the act is to mandate participation in the National Flood Insurance Program as a condition for receiving federal aid in financing the construction, purchase, repair, or improvement of a building or mobile home located in a flood hazard area (SPFA).

Further amendment to the Act was passed in 1974 requiring all federally regulated or insured lenders to notify a prospective borrower, before settlement, if the property securing the loan was located in a special flood hazard area. Essentially this means that the lender now had to make sure there was a flood insurance policy in effect on the loan if the property was in a special flood hazard area. A further amendment to this Act in 1977 made it mandatory for the lender to notify borrowers whether they would be eligible for federal disaster assistance in the event of a declared flood disaster.

The act was again revised in 1994 (National Flood Insurance Reform Act) to broaden the mandatory flood insurance requirements of the NFIP, placing primary responsibility for ensuring compliance with the act on lenders by compelling them to do the following:

- Follow more disciplined initial borrower notification requirements.
- Force-place the required flood insurance for borrowers who do not purchase or maintain it.
- Escrow flood insurance premiums on residential and mobile home loans along with escrows for taxes and insurance.
- Document a determination that a mortgaged property is flood prone.

Under NFIA, once a community has been declared to be in a special flood hazard area by the FEMA (including mudslide, or flood erosion risk), it has one year in which to become a participant in the National Flood Insurance Program, or no federal financial assistance will be forthcoming. The importance of this to lenders is that flood insurance is required on any loan secured by a property where any portion of the structure is located in a special flood hazard area where the community is participating in the National Flood Insurance Program. Essentially the burden of determining whether the location of the property is in a special flood hazard area rests on the lender.

Requirements

Flood Insurance is required on loans made by federally regulated lending institutions if the following criteria exist:

- The community in which the property is located is participating in the National Flood Insurance Program; and
- Any portion of the structure on the property securing the loan is located in a special flood hazard area.

Properties Eligible for NFIP Coverage

Any walled or roofed structures other than gas or liquid storage tanks, that are above ground and affixed to a permanent site are eligible properties under the National Flood Insurance Program. Most buildings under construction are also eligible for coverage. Manufactured homes are eligible for coverage if they are on permanent foundations and anchored to resist floatation, collapse, or lateral movement. Among properties that are **NOT** eligible for coverage are recreational vehicles, park trailers and travel trailers. Separate flood policies are required for each individual building, although coverage is extended to detached garages and carports that service the insured dwelling. For condominiums, a Residential Condominium Building Association Policy is available through the homeowners associations.

Lender Compliance

Federally regulated lenders must ensure flood insurance is in place at closing and for the entire term of the loan for mortgages secured by structures located in a special flood hazard area. The burden of determining whether the location of the property is in a special flood hazard area is on the lender, even when a third-party flood determinations company is used to make the determination.

Under the reforms instituted by the 1994 Revision, lender responsibilities include the following:

- Determining whether the building offered for security is, or will be, located in a special flood hazard area (SFHA);
- Documenting the determination of flood hazard status
- Requiring that flood insurance to the appropriate limit is obtained when necessary; and
- During the term of the loan, ensuring that flood insurance is maintained or added if the lender becomes aware that the building involved subsequently becomes part of an SFHA.

When a lender determines that a property is in a SFHA, they must notify the borrower who is purchasing the property of the following:

- The property to be held as security on the loan is located in a special flood hazard area.
- Flood Insurance is required in order for the lender to make the loan and should be for the principal amount of the loan or the maximum amount available under NFIP.
- Whether or not federal disaster relief will be available in the event of damage to the property from a flood.

The notice to the borrower must contain specific language and must be delivered to the borrower prior to the closing of the loan. The lender should be named as mortgagee on the policy to protect the lender's interest in the event of damage to the building. The flood insurance coverage must be in place at the time of closing and must be maintained for the term of the loan. If the lender at any time determines that the coverage has lapsed and the borrower refuses to reinstate the policy, the lender must force-place insurance on the loan.

Administration and Enforcement

The National Flood insurance Act is administered by the Federal Insurance Agency (FIA), working with FEMA. Enforcement responsibility with regard to the mortgage banking industry is carried out by the OCC, FDIC, OTS, NCUA and the Board of Governors of the Federal Reserve System.

VI. Home Mortgage Disclosure Act (HMDA)-- Regulation C

The Home Mortgage Disclosure Act and its implementing body Regulation C was enacted in 1975 to achieve the following goals:

1. To provide the public with information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located;
2. To help public officials distribute public-sector investments so as to attract private investment to areas where it is needed; and
3. To identify possible discriminatory lending patterns and enforce anti-discrimination statutes by requiring the collection and disclosure of data about applicant and borrower characteristics.

In 1993 the Act was expanded by amendments in the Federal Deposit Insurance Corporation Improvement Act of 1991 to include coverage of independent mortgage bankers. The amendment requires that all covered institutions must report the race or national origin, sex, and income of the applicant or borrower. This fair lending aspect of HMDA requires the collection, reporting, and disclosure of data regarding applicant and borrower characteristics, in order to identify possible unfair lending patterns and to help enforce anti-discrimination statutes.

Reg. C now applies to almost all financial institutions, including commercial banks, savings banks, credit unions, and mortgage lending institutions, including majority owned subsidiaries of depository institutions.

Disclosure Requirements

Under HMDA, financial institutions are required to collect data regarding the application and origination of home purchase and home improvement loan (including refinancing) for each calendar year. The institutions must:

1. Report certain data about each application or loan (such as type and amount) and about the location of the dwelling to which it relates.
2. Report the race or national origin, sex, and income of the applicant or borrower. This requirement does not apply to banks, thrifts or credit unions that have assets of \$30 million or less.

For brokered (wholesale) loan applications, HMDA requires the lender to report the loan applications that the lender approved (or denied) and subsequently acquired according to a pre-closing arrangement (whether or not they closed in the lender's name). These reports must be submitted in a format prescribed by Regulation C. The reports must then be submitted to the appropriate federal supervisory agency by March 1 following the calendar year for which the loan data are compiled.

Supervisory Agencies and Enforcement

The agencies charged with the collection of HMDA data include the OTS, OCC, the Federal Reserve Banks (FRB), the FDIC, the NCUA, and the U.S. Department of Housing and Urban Development (HUD). Enforcement is carried out by the FDIC.

VII. The Home Owners Protection Act of 1998 HOPA

The Home Owners Protection Act of 1998 (HOPA) requires that private mortgage insurance (PMI) be cancelled when a loan reaches certain, specific thresholds. The Act's MI cancellation policy applies to privately insured first mortgages on single family primary residences closed after July, 29th 1999.

This law includes two basic consumer protections:

- Requires lenders to inform borrowers—both at closing and annually—about their right to request cancellation of their mortgage insurance.
- Requires lenders to automatically cancel insurance for those who do not request cancellation.

Without the law, PMI is generally cancelable once a homeowner builds up enough equity in the home. Government Sponsored Entities such as Fannie Mae and Freddie Mac however set their own cancellation requirements.

Disclosures

The law calls for two disclosures to be made to the borrower in connection with the cancellation process.

- **Initial Disclosure**—Lenders must give borrowers a written notice at closing that explains that PMI is part of their mortgage and that they have the right to have it canceled at a certain point.
- **Annual Disclosure**—Lenders must send borrowers an annual reminder that they have Private MI and have the right to request cancellation once they've met cancellation requirements.

Homeowner Protection Act Cancellation Requirements

Under HOPA, There are two circumstances under which PMI must be cancelled:

- **Borrower-Initiated Cancellation**—A lender must cancel PMI at the request of a borrower whose mortgage balance is 80 percent of the original value of the home securing the loan. The borrower must be up to date on mortgage payments and have no other loans on the house. The lender must be satisfied that the property value has not declined.
- **Automatic Termination**—For most insured loans PMI will be cancelled automatically when the mortgage balance is at 78 percent of the original value of the house. The borrower must be up to date on mortgage payments, otherwise insurance must be cancelled automatically once the borrower becomes current.

VIII. The Privacy Act – Regulation P

On November 12, 1999, The Privacy of Consumer Financial Information Act, also known as the Graham-Leach- Bliley Act (GLBA) or Regulation P, was signed into law. The Act places restrictions on the information management of financial institutions by prohibiting, under certain conditions, the sharing of a consumer’s non-public personal information (NPI) with non affiliated third parties. Compliance with the Act became mandatory on July 1, 2001.

This Act applies to all financial institutions. The following is a brief list of the types of Financial Institutions that the Act encompasses: mortgage broker or lender, check cashier, credit counseling service, financial or investment advisory service, retailer that issues its own credit card, auto dealers that lease or finance, collection agency, government entities that provide financial products such as student loans or mortgages.

Under the provisions of the act all financial institutions are required to do the following:

- provide an initial privacy notice to the customer at the time that a customer relationship is established;
- Provide and opt-out notice prior to sharing nonpublic personal information with nonaffiliated third parties.
- Provide customers with a “reasonable opportunity” to opt out before disclosing nonpublic personal information about them to nonaffiliated third parties.
- Provide an annual privacy notice annually for the duration of the customer relationship.
- If a customer elects to opt out of all or certain disclosures, the financial institution must honor that opt-out direction as soon as reasonably practicable after the opt-out is received.
- If privacy practices are changed such that the most recent privacy notice provided to the consumer is no longer accurate, the financial institution must provide new revised privacy and opt out notices.

Non Public Personal Information

Non Public Personal Information (NPI) is defined as any information that is non-public in nature and is personally identifiable. NPI includes any list, description, or other grouping of consumers (and publicly available information pertaining to them) derived using any personally identifiable financial information that is not publicly available.

This information may be obtained from the following sources common to the mortgage industry:

- Applications and Registrations
- Information obtained in the process of verifying information that is provided on an application or registration
- Information that is obtained through a credit reporting agency
- Information that may be obtained from consumer providers to develop competitive marketing programs for our customers and clients.

Compliance

Publicly Available Information

Publicly Available Information is:

Any information that a financial institution has a reasonable basis to believe is lawfully made available to the general public from:

- Federal, State, of local government records
- Widely distributed media
- Disclosures to the general public required by Federal, State, or local law.

Relationship to State Law

As a final note, Regulation P in no way preempts State laws except to the extent that they are "inconsistent" with this federal law. A state law is "inconsistent" if it affords "greater protection" to consumers than provided for by this federal law, as determined by the Federal Trade Commission (FTC).

IX USA Patriot Act

The USA Patriot Act of 2001, Section 326, requires that financial institutions implement procedures to obtain, verify and record information that identifies each applicant who opens an account. These procedures are referred to as the Customer Identification Program (CIP). CIP regulation, 31 CFR 103.21, applies to federally regulated banks and savings associations, including branches and agencies of foreign banks in the United States, credit unions, and non federally regulated private banks, trust companies and credit unions. To ensure that Lexington Lending's brokers and correspondents comply with the law, the following procedures were effective October 1, 2003.

1. Identity Verification Procedures¹

a) Face-to-face applications:

All wholesale lenders submitting applications must include for all applicant(s):

- Identifying information (borrower name, address, date of birth and Social Security number) for each applicant, and
- Wholesale lenders must use unexpired government –issued piece(s) of identification, evidencing verification of the applicant(s) bearing a photograph or similar safeguard, and
- complete form #3243 Patriot Act Certification Form. A similar document may be used.

b) Internet, mail, and phone applications²

Internet:

All applicants must provide the identifying information (borrower name, address, date of birth and Social Security number) on the credit application. If the identifying information is not completed, the application is considered incomplete and must be requested from the sender.

Mail:

All applicants must provide the identifying information (borrower name, address, date of birth and Social Security number) on the credit application. If the identifying information is not completed, the application is considered incomplete and must be returned to the sender.

Phone:

The interviewer must request the identifying information (borrower name, address, date of birth and Social Security number) from the applicant(s) and record the information on the credit application. If the identifying information is not completed, the application is considered incomplete and must be returned.

¹ These procedures are for consumer loans, which are only made to natural persons.

² The nondocumentary methods will be used to verify the identifying information (borrower name, address, date of birth, and Social Security number) on the credit application. (e.g., contacting the customer; verifying the customer's identity through the comparison of information obtained from a consumer reporting agency)

Compliance

If the applicant(s) identifying information is not sent at the time of underwriting submission, the information will be required as a prior to closing condition.

2. Acceptable Identification Documentation³

Acceptable identification documentation for U.S. and non-U.S. persons and other forms of government-issued identification include:

Acceptable Primary Identification—Generally, acceptable primary identification will consist of unexpired government issued photo identification listed below.

- Valid permanent driver's license.
- Valid U.S. passport.
- Valid U.S. military identification card.
- Valid resident alien card.

Acceptable Secondary Identification—TWO pieces must be presented.

- Valid state identification card.
- Valid out-of-state driver's license.
- Along with ONE of the following: birth certificate, current car registration, current pay stub or utility bill with name and address matching the applicant's ID.

Acceptable Identification for NON-U.S. Persons—TWO pieces must be presented.

- Valid permanent resident card.
- Valid resident alien card (not expired).
- Valid U.S. citizen identification card.
- Valid employment authorization card.
- Valid temporary resident card (not expired).
- Valid non-resident alien boarder crossing card.
- Valid non-U.S. passport (not expired).
- Valid non-immigrant visa and border crossing card.
- Along with ONE of the following: current car registration, current pay stub or utility bill with name and address matching the applicant's ID.

3. Lack of or Insufficient Identification Verification

Circumstances that may result in Lexington Lending's denial of the application are:

- Inability to obtain un-expired acceptable identification documentation described in #3 above, or inability to obtain a lender-signed statement described in #6 below.
- Lack of familiarity with the documents presented which cannot reasonably be used to verify the information.
- Presence of evidence of fraud.
- Presence of one or more of the above circumstances

4. Retention of Identifying Information

³ The underwriter is permitted to verify identity and accept other forms of government-issued unexpired identification, which includes a photograph or accept secondary forms of identification.

Compliance

- Identifying information (borrower name, address, date of birth and Social Security number) will be retained for five years after the asset (account) is sold to another lender,⁴ or paid-off.
- Verifying documents (e.g., driver's license) will be retained for five years after the date of funding.
- If applicable, a description or evidence of the resolution of discrepancies verifying the identifying information will be retained for five years after the account is sold to another lender or paid-off.

5. Form #3243 or a similar form should be used when verifying and recording identifying information:

Wholesale Lending Adequate Customer Notice

All brokers and correspondents are responsible for the disclosure requirements set forth in this part of the Patriot Act. The following language must be communicated in a manner that is logically designed so that an applicant(s) is able to at least hear or view this verbiage prior to account opening.

The sample language is as follows:

IMPORTANT INFORMATION ABOUT PROCEDURES FOR OPENING A NEW ACCOUNT—"To help the government fight the funding of terrorism and money laundering activities, federal law requires all financial institutions to obtain, verify and record information that identifies each person who opens an account. What this means for you: When you open an account, we will ask for your name, address, date of birth, and other information that will allow us to identify you. We may also ask to see your driver's license or other identifying documents."

Filing of Suspicious Activity Report:

- If there appears to be evidence of fraud, Lexington Lending will file a Suspicious Activity Report (SAR)
- Lexington Lending has obtained notification from a government authority (e.g., FBI, OTS) and must file a SAR.

Note: Upon notification of the creation of any list as defined in Section 326 of the Customer Identification Program (CIP) of known or suspected terrorist organizations issued by any federal government agency, these procedures will be amended accordingly for compliance.

Post-Loan Closing

Lexington Lending has the option to close and request for repurchase from the broker or correspondent:

- Any loan that is found to contain evidence of fraud.
- A loan where the applicant(s) appears on a list or notice of suspicion from a government authority.

The introducing wholesale lender is required to follow this procedure for all applications submitted on and after October 1, 2003.

⁴ Credit denials or withdrawn applications are not considered accounts since no formal relationship is established with the applicant.