Higher Priced Mortgage Loan Proposed Rule

On July 10, 2013 the FDIC, Federal Reserve and four other agencies introduced a proposed rule to exempt higher priced mortgage loans from the appraisal requirements. These loans include loans where the interest rate is priced with an annual percentage rate that exceeds the average prime offer rate by a specified percentage.

"The Agencies are proposing amendments to the Final Rule implementing these requirements; specifically, the Agencies are proposing exemptions from the rules for: (1) transactions secured by existing manufactured homes and not land; (2) certain "streamlined" refinancings; and (3) transactions of $25,000 or less. " *Excerpt from the joint release dated July 10, 2013.*

The stated intent is to "save borrowers time and money and to promote the safety and soundness of creditors." It is obvious that the first part of that intent would be achieved as the borrowers would certainly save on closing costs and the process would be sped up. However, are we throwing out due diligence for the sake of expediting the loan process? I am still pondering how this proposed rule promotes safety and soundness for the creditor. On what basis will the loan amount be determined? Would the lender rely on the homeowner's assessment, Tax Assessor Records, or Automated Valuation Systems?

While some of the proposed rule changes seem appropriate, specifically the streamlined refinances, there seems to be a memory loss of the past 5 years. The subprime loans were certainly higher priced mortgages. The loan amount threshold of $25,000 seems low in comparison to most mortgage loans. History has also shown these thresholds get moved over time once there is a bar set. It seems this rule would have a direct affect in the home equity market. Second mortgage loans would be higher risk to the creditor and not having a clear equity position does not seem to improve the safety or the soundness of the creditor.

It is agreed that there is a need in the market for a streamlined process for these types of mortgage products. Technology might have a place in satisfying this need, but only as a beginning point. Automated Valuation Models (AVM) are limited in that that they have no way to identify the quality and condition of the home. Comparable Data Selection usually provides a wide swing in sold prices. They also have no way of determining if the home even exists. More recently, models have been enhanced with drive by inspections by qualified people that can rate quality, condition and external factors that might have an effect on the value such as busy roads, proximity to railroads or unsightly views. I recently had an occasion to follow up on an AVM where the value estimated seemed reasonable. However, after driving by the site, I found that the site was adjacent to an active railroad, was next door to a school bus repair facility and on a very busy road. Prudent lending should include having "put some eyes on the property" so assure that there are no unusual conditions.

However this proposed rule is finalized, the Real Estate Lending Industry would do well to remember why the Frank Dodd Act and Wall Street Reform were needed in the first place.

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FHFA.Gov Link to Proposal Notice
http://www.fhfa.gov/webfiles/25354/Appraisal_reqrmnt_exempts_FR_Notice_1_PR_Vsn.pdf