

# Legislative Analysis

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## **PREDATORY LENDING:**

**House Bill 5294 (Substitute H-1)**  
**Sponsor: Rep. Mike Simpson**

**House Bill 5295 (Substitute H-1)**  
**Sponsor: Rep. Steve Tobocman**

**House Bill 5296 (Substitute H-1)**  
**Sponsor: Rep. Tim Melton**

**House Bill 5297 (Substitute H-1)**  
**Sponsor: Rep. Kathy Angerer**

**House Bill 5299 (Substitute H-1)**  
**Sponsor: Rep. Brenda Clack**

**House Bill 5300 (Substitute H-1)**  
**Sponsor: Rep. Marc Corriveau**

**House Bill 5301 (Substitute H-1)**  
**Sponsor: Rep. Edward Gaffney, Jr.**

**House Bill 5302 (Substitute H-1)**  
**Sponsor: Rep. Kate Ebli**

**House Bill 5303 (Substitute H-1)**  
**Sponsor: Rep. Brian Calley**

**House Bill 5307 (Substitute H-1)**  
**Sponsor: Rep. Coleman Young**

**House Bill 5308 (Substitute H-1)**  
**Sponsor: Rep. Mary Valentine**

**Committee: Banking and Financial Services**

**Complete to 6-16-08**

## **A SUMMARY OF PROPOSED SUBSTITUTES FOR HOUSE BILLS 5294-5297, 5299-5303, AND 5307-5308**

**BRIEF SUMMARY:** As a package, the bills would do the following:

- Rename the Consumer Mortgage Protection Act as the Home Loan Protection Act (HLPAct) and include high-cost home loans.
- Exempt depository institutions from regulation under the HLPAct.
- Prohibit a creditor from extending a home loan unless the borrower was reasonably determined to be able to repay the loan.
- Prohibit a creditor from making a high-cost home loan without documentation that the borrower received counseling on the advisability of the loan.
- Prohibit the charging of prepayment fees or penalties.
- Prohibit certain conduct by a creditor.
- Prohibit class action suits against a creditor.

- Subject purchasers of high-cost home loans on the secondary market to the same liability, with some restrictions, as the original lender.
- Require high-cost home loans sold on the secondary market to have a notice attached to the document warning that liability could attach to the purchaser for all claims and defenses of the borrower.
- Provide a "good faith" exception to creditors and assignees of a home loan who failed to comply with the act's provisions but who corrected the situation within certain timeframes.
- Prohibit "bad faith" attempts to avoid application of the HLPA.
- Revise civil fine penalties for violations of the HLPA.
- Create a criminal penalty for knowingly violating the HLPA.
- Apply the HLPA to any home loan or other transaction governed by the act that concerned real property located within the state.
- Apply requirements, as well as penalties and remedies, of the HLPA concerning home loans to persons licensed or registered under the Mortgage Brokers, Lenders, and Servicers Licensing Act and the Secondary Mortgage Loan Act.
- Define new terms and revise or eliminate others.

House Bills 5294-5297 and 5299-5303 are tie-barred to each other and House Bills 5307 and 5308 are tie-barred to 5294-5297 and 5299-5303, meaning that no single bill could take effect unless all are enacted. All the bills except for House Bills 5307 and 5308 would amend the Consumer Mortgage Protection Act. A detailed description of each bill follows.

## **DETAILED SUMMARY OF BILLS:**

### **House Bill 5294**

The bill would amend the title of the Consumer Mortgage Protection Act (CMPA) (MCL 445.1631 and 445.1632) to apply the act to high-cost home loans. The bill would also rename the act as the "Home Loan Protection Act" (HLPA) and exempt a depository financial institution, or its operating subsidiary, from regulation under the act.

Primarily, the bill would define new terms, revise the definitions of several terms, and eliminate several other terms. "Home loan" would replace the term "mortgage loan," and would mean a closed-end or open-end credit plan or other extension of credit that did not exceed the maximum original principal obligation, met the requirements for a federally

related mortgage loan under federal regulations, and was not a reverse mortgage transaction or a loan primarily for business, agricultural, or commercial purposes.

A "high-cost home loan" would mean a home loan where the terms of the loan met or exceeded one or more thresholds, with "threshold" meaning a rate threshold or a total points and fees threshold—both terms are defined in the bill.

### **House Bill 5295**

The bill would amend sections of the HLP (MCL 445.1633 and 445.1634) to prohibit certain conduct on the part of a creditor. "Creditor" would be defined by House Bill 5294 as meaning a lender as that term is defined under federal law (24 CFR 3500.2) or a mortgage broker; "creditor" would replace the term "lender" in the act, and "home loan" would replace "mortgage loan".

The bill would prohibit certain conduct on the part of a creditor, including the following:

- Extending a home loan to a borrower unless the creditor reasonably determined, as specified in the bill, that the borrower was able to repay the loan according to the loan terms. Use of an automated underwriting system complying with the act's provisions would constitute a reasonable method for determining a borrower's ability to repay a home loan.
- Knowingly or intentionally refinancing an existing home loan if the new loan did not have a reasonable, tangible net benefit to the borrower when specified circumstances were considered.
- Steer, counsel, or direct a consumer to rates, charges, principal amounts, or prepayment terms that were not reasonably advantageous to the borrower.
- Materially mischaracterize a borrower's credit history or the home loans available to a borrower from the creditor.
- Materially mischaracterize the appraisal value of a dwelling.
- If unable to suggest, offer, or recommend a reasonably advantageous home loan, discourage the borrower from seeking a home loan from another creditor.
- Charge or collect any prepayment fee or penalty on a home loan; a prepayment penalty provision would be void and unenforceable.

The bill would also regulate the manner in which a creditor could charge late payment fees and fees for informing a person of the balance due to pay off a home loan.

### **House Bill 5296**

The bill would amend the HLP (MCL 445.1635). Currently, Section 5 prohibits a mortgage loan with a term of less than five years from having a payment schedule with regular periodic payments that, when aggregated, do not fully amortize the outstanding principal balance. The bill would delete this provision.

Instead, Section 5 would subject a high-cost loan to several limitations and prohibited practices in addition to other requirements contained in the act. Under the bill, a creditor, in relation to a high-cost home loan, could not:

- Make a loan without receipt of a certification documenting that the borrower had received counseling from an approved nonprofit organization on the advisability of the loan transaction.
- Include in the loan documents for a high-cost home loan, or charge a borrower, any prepayment fees or penalties.
- Pay a contractor for home improvements from the proceeds of a loan unless the payment was payable to the borrower, or to both, or to an escrow account as specified in the bill.
- Charge a fee to modify, renew, extend, or amend a loan or defer any payment due under the loan terms.
- Finance points or fees in excess of 2 percent of the loan amount.

In addition, restrictions would be placed on a high-cost home loan. Among other restrictions, the regularly scheduled periodic payments would have to cover the full amount of interest due, and the loan provisions could not increase the interest rate after default. In addition, a high-cost home loan document creating a debt or an interest in property to secure a debt would have to include a notice printed conspicuously on the face of the document that stated it was a high-cost home loan subject to special rules under state laws and that a purchaser or assignee could be liable for all claims and defenses of the borrower.

### **House Bill 5297**

The bill would amend the HLPA (MCL 445.1636 and 445.1637). Currently, when a person applies for a mortgage loan, the lender is required to provide the applicant with the "Borrowers Bill of Rights," a document which outlines various rights such as the right to be informed about the total cost of the loan, and also a written notice entitled "Consumer Caution and Home Ownership Counseling Notice" regarding the value of receiving credit counseling before taking out the loan. The bill would delete from the Borrowers Bill of Rights a reference to the HUD settlement costs booklet "Buying Your Home" and delete from the written notice regarding counseling a reference to HUD's counseling hotline.

### **House Bill 5299**

The bill would add two new sections to the HLPA (MCL 445.1637c and 445.1637d) regarding sales of high-cost home loans on the secondary market. A person who purchased or was assigned a high-cost loan would be subject to all affirmative claims and any defenses with respect to the loan that the borrower could assert against the original creditor of the loan. The bill would provide an exemption from this liability if the purchaser or assignee demonstrated by a preponderance of the evidence that (1) it had a policy in place at the time of the purchase or assignment expressly prohibiting its purchase or acceptance of assignment of any high-cost loans; (2) required by contract that

a seller or assignor of home loans to the purchaser or assignee represent and warrant that the seller or assignor would not sell or assign any high-cost home loans to that purchaser or assignee or that the seller or assignor was a beneficiary of a representation and warranty from a previous seller or assignor to that effect; and (3) exercised reasonable due diligence at the time of purchase or assignment of home loans or within a reasonable period of time after the purchase or assignment, to prevent the purchase or taking assignment of any high-cost loans. Reasonable due diligence would have to provide for sampling and would not require loan-by-loan review.

The bill would limit the amount that a borrower could assert in a claim against any subsequent holder or assignee of the home loan to the monthly payments already paid, finance charges other than those already collected in the monthly payments, forfeiture of future interest on the loan, reasonable costs, and reasonable attorney fees. A claim would have to be made within five years of the closing of a high-cost home loan for a violation of the act in connection with the loan as an original action. Any defense, claim, or counterclaim could be mounted at any time during the life of the loan after an action to collect on the home loan or foreclosure on the collateral securing the home loan had been initiated, or after the debt arising from the home loan had been accelerated or the home loan had become 60 days in default.

The above provisions would be independent of each other and would not limit each other, but could not be construed to limit the substantive rights, remedies, or procedural rights available to a borrower against any creditor, assignee, or holder under any other law.

If a person was found by a preponderance of the evidence to have violated the act, the court could award all of the following to the borrower in a civil action:

- Actual damages, including consequential and incidental damages.
- For violations of the provisions of House Bill 5295 regarding prohibited conduct on the part of creditors and restrictions on high-cost home loans, statutory damages as specified in the bill. (The bill also refers to a violation of Section 4a; that section, which required a creditor to determine a borrower's ability to pay, would have been added by House Bill 5296 as introduced, but was eliminated in the H-1 substitute.)
- Punitive damages if the violation was malicious or reckless.
- Costs and reasonable attorney fees.

In addition, an action for injunctive, declaratory, and any other equitable relief could be brought to enforce compliance with the act by the state attorney general, a county prosecutor, or a borrower. The remedies provided in the bill would be cumulative and not the exclusive remedies available. A borrower could proceed under the bill's provisions without having to first exhaust available administrative remedies. A borrower could only assert a claim under the act on his or her own behalf and could not assert claims on behalf of similarly situated borrowers.

The bill would also extend the right of rescission granted to a borrower under the federal Truth in Lending Act for a violation of that act as a way of recoupment against a party foreclosing on the home loan or collecting on the loan at any time during the term of the

loan. This would not limit any recoupment right available to a borrower under any other law.

A creditor or assignee who failed to comply with the provisions of the HPLA while acting in good faith would not be considered in violation of the act if either of the following were established: (1) the creditor or assignee made appropriate restitution to the borrower and appropriate adjustments to the loan within 60 days of the loan closing and before receiving any notice of the compliance failure; or, (2) the compliance failure was not intentional and resulted from a bona fide error, as explained in the bill, and the borrower was notified, appropriate restitution was made, and appropriate adjustments to the loan were made within 90 days of the loan closing and before receiving any notice of the compliance failure.

A provision in an agreement for a home loan allowing a person to require a borrower to assert a legal claim or defense in a forum located in a state other than Michigan or that limited in any way a claim or defense granted to a borrower would be void and unenforceable. Further, dividing a home loan transaction into separate parts, structuring a home loan transaction as an open-end loan for purposes of evading the HPLA, or engaging in any other subterfuge with the intent of evading the HPLA would be considered in bad faith and would be prohibited.

#### **House Bill 5300**

The bill would amend the HPLA (445.1638 and 445.1639) to allow the commissioner of the Office of Financial and Insurance Regulation (OFIR) to promulgate rules under the Administrative Procedures Act as necessary to implement and administer the act. The commissioner could provide guidance to any person over which the commissioner had regulatory authority on the application of and compliance with the HPLA.

#### **House Bill 5301**

The bill would amend Sections 10 and 11 of the HPLA (445.1640 and 445.1641). Currently, Section 10 provides that the attorney general or county prosecutor for the county in which an alleged violation of the act occurred may bring an action to obtain a declaratory judgment that a method, act, or practice was a violation; enjoin a person who was engaging or was about to engage in such acts; and/or obtain a civil fine of not more than \$10,000 for a first offense and not more than \$20,000 for a second or subsequent offense.

The bill would delete the underlined portion and add that in addition to any other remedies or penalties imposed by the act, a person who violated the act or an order made or rule promulgated under the act, or who directly or indirectly counseled, aided, or abetted in a violation would be responsible for a civil fine of not more than \$3,000 for each violation, not to exceed \$30,000 for a transaction resulting in more than one violation, plus the costs of investigation. This penalty would apply to a creditor, a member, officer, director, or employee of a creditor, or any other person.

Further, Section 11 currently does not count certain unintentional errors or acts as violations if the violations were corrected within 60 days after discovery. That provision would be deleted. Instead, Section 11 would make it a misdemeanor punishable by a fine of not more than \$15,000 and/or imprisonment for not more than one year for a creditor, a member, officer, director, or employee of a creditor, or any other person, to knowingly violate the HLPAs or an order made or rule promulgated under the act.

### **House Bill 5302**

The bill would amend the HLPAs (445.1642 and 445.1643) to specify that the rights conferred by the act would be independent of and in addition to any other rights under state or federal law. The bill would also apply the HLPAs to any home loan or other transaction governed by the act concerning real property located within the state.

The bill would eliminate a provision requiring the Office of Financial and Insurance Services to develop and make available to local governments, financial institutions, and other interested persons a model program or programs for financial education.

### **House Bill 5303**

This bill would also amend the HLPAs (445.1644 and 445.1645). Section 14 states that the federal government and the state have sole regulatory responsibility over home loans made within the state and the manner in which that business is conducted; the section also preempts certain actions of local governments. The bill would delete a provision specifying that the illegality or invalidity of any provision of Section 14 would not affect any legal and valid provision or application of the entire section (which made the provisions and applications of the section severable). Further, the bill would replace the term "mortgage loans" with "home loans."

### **House Bills 5307 and 5308**

House Bill 5307 would amend the Mortgage Brokers, Lenders, and Servicers Licensing Act (MCL 445.1672 and proposed 445.1674a). To the list of 14 prohibited actions on the part of a person licensed or registered under the act, the bill would add that a licensee or registrant could not fail or neglect to do any of the following in connection with the brokering, servicing, or making of any mortgage loan:

- Act in good faith and with fair dealing in any transaction, practice, or course of business.
- Safeguard and account for any money handled for the borrower.
- Follow reasonable and lawful instructions from the borrower.
- Use reasonable skill, care, and diligence.
- Disclose clearly and in a timely manner to the borrower material information that might reasonably affect the borrower's rights, interests, or ability to receive the intended benefit from the mortgage loan, including the total compensation the broker would receive from any of the loan options the licensee or registrant presented to the borrower.

- Make reasonable efforts to secure a mortgage loan that was reasonably advantageous to the borrower considering all the circumstances, including the rates, charges, and repayment terms of the loan.

The above listed duties and standards of care could not be waived or modified.

Further, the bill would add a new section to specify that the Home Loan Protection Act applies to a licensee or registrant under the Mortgage Brokers, Lenders, and Servicers Licensing Act, and would require a licensee or registrant to comply with the requirements of the HLP Act in connection with any home loans. A licensee or registrant would also be subject to the remedy and penalty provisions of the HLP Act for a violation of the 14 prohibitions currently contained in Section 22.

House Bill 5308 would similarly amend the Secondary Mortgage Loan Act (493.74 and proposed 493.74a) to apply to licensees and registrants under that act making secondary mortgage loans.

#### **FISCAL IMPACT:**

The bills would have no material budgetary impact on the Office of Financial and Insurance Regulation or the Department of Labor and Economic Growth, although the additional restrictions placed on lenders would be subject to review during the course of OFIR's periodic investigations of mortgage licensees.

House Bill 5300 provides OFIR with the authority to promulgate administrative rules. These costs wouldn't be significant. House Bill 5301 alters the structure of civil fines imposed for violations of the act. (This penalty structure would be consistent with the structure of penalties under the mortgage licensing acts.) Additionally, House Bill 5101 imposes a civil fine of not more than \$15,000 and/or imprisonment for not more than one year for knowingly violating the act, an order, or administrative rule. The fiscal impact would depend on the number and severity of misdemeanor sentences, which generally are a local responsibility. There are no data to indicate how many offenders might be affected by the bills. To the extent that more offenders were convicted of misdemeanors and sentenced to local sanctions, local units of government would incur increases costs of misdemeanor probation supervision and jail incarceration, both of which vary by county. Any increase in penal fine revenue would benefit local libraries, which are the constitutionally-designated recipients of those revenues.

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