CUNA REGULATORY ADVOCACY

CUNA REGULATORY COMMENT CALL

July 17, 2012

CFPB Proposed Rule to Implement Recent Changes to the Home Ownership and Equity Protection Act (HOEPA)

EXECUTIVE SUMMARY

- The Dodd-Frank Act amends the Truth in Lending Act by expanding the types of mortgage loans that are subject to the protections of the Home Ownership and Equity Protection Act of 1994 (HOEPA), by revising and expanding the triggers for coverage under HOEPA, and by imposing additional restrictions on HOEPA mortgage loans, including a pre-loan counseling requirement. The Dodd-Frank Act also amends the Truth in Lending Act and the Real Estate Settlement Procedures Act by imposing certain other requirements related to homeownership counseling.
- The Consumer Financial Protection Bureau (CFPB) is proposing to amend Regulation Z (Truth in Lending Act (TILA)) and Regulation X (Real Estate Settlement Procedures Act (RESPA)) to implement the Dodd-Frank Act's amendments to TILA and RESPA.
- The proposal would implement revised HOEPA thresholds; HOEPA threshold would be triggered where:
  - A loan's annual percentage rate (APR) exceeds the average prime offer rate (APOR) by 6.5 percentage points for most first-lien mortgages and 8.5 percentage points for subordinate-lien mortgages;
  - A loan's points and fees exceed 5% of the total loan amount, or a higher threshold for loans below $20,000; or
  - The creditor may charge a prepayment penalty more than 36 months after loan consummation, or penalties that exceed more than 2% of the amount prepaid.
- The CFPB is has issued a separate proposed rulemaking to integrate RESPA and TILA disclosures, which proposes to broaden the definition of "finance charge" under Regulation Z. If such an expanded definition is adopted, it will cause more loans to exceed the APR and points and fees triggers and be classified as high-cost mortgages under HOEPA. This Comment Call addresses the amendments to HOEPA's high-cost triggers.
- In addition, the proposal would implement new Dodd-Frank Act restrictions and requirements concerning loan terms and origination practices for high-cost mortgage, including the following changes:
  - Balloon payments would largely be banned, and creditors would be prohibited from charging prepayment penalties and financing points and fees;
  - Late fees would be restricted to 4% of the payment that is past due, fees for generation of payoff statements would be restricted, and fees for loan modification or loan deferral would be banned;
  - Creditors originating open-end credit plans would be required to assess consumers' ability to repay the loans;
  - Creditors and mortgage brokers would be prohibited from recommending or encouraging a consumer to default on a loan or debt to be refinanced by a high-cost mortgage loan; and
  - Before making a high-cost mortgage loan, creditors would be required to obtain confirmation from a federally certified or approved homeownership counselor that the consumer has received counseling on the advisability of the loan.
- Also, the proposal would implement two Dodd-Frank Act homeownership counseling-related provisions that are not amendments to HOEPA. The proposal would amend Regulation X to implement a requirement under RESPA that lenders provide a list of federally approved homeownership counselors or counseling organizations to consumers. It would also amend Regulation Z to implement a requirement under TILA that creditors obtain confirmation that a first-time borrower has received homeownership counseling.
- The CFPB is accepting public comments until September 7, 2012. **Please send your comments to CUNA by August 20.**

Please send comments to Senior Vice President and Deputy General Counsel Mary Dunn and Assistant General Counsel Luke Martone. Click here for the proposed rule.

BACKGROUND

The Dodd-Frank Act amends the Truth in Lending Act by expanding the types of mortgage loans that are subject to the protections of the Home Ownership and Equity Protection Act of 1994 (HOEPA), by revising and expanding the triggers for coverage under HOEPA, and by imposing additional restrictions on HOEPA mortgage loans, including a pre-loan counseling requirement. The Dodd-Frank Act also amends the Truth in Lending Act and the Real Estate Settlement Procedures Act by imposing certain other requirements related to homeownership counseling. The CFPB is proposing to amend Regulation Z (Truth in Lending) and Regulation X (Real Estate Settlement Procedures Act) to implement the Dodd-Frank Act's amendments to the Truth in Lending Act and the Real Estate Settlement Procedures Act.

In addition to this proposal, the CFPB currently is engaged in six other rulemakings relating to mortgage credit to implement requirements of the Dodd-Frank Act that are in the proposed or pre-proposed stage: TILA-RESPA integration; servicing; loan originator compensation; appraisals; ability to repay; and escrows. With the exception of the TILA-RESPA rulemaking, the Dodd-Frank requirements for these rulemakings generally become effective January 21, 2013.

Corrections and Unintentional Violations of HOEPA

The Dodd-Frank Act amends TILA to allow a creditor or assignee of a high-cost mortgage in certain circumstances to correct a failure to comply, when acting in good faith, with HOEPA requirements. However, the CFPB is currently not proposing to issue regulatory guidance concerning this provision.

DESCRIPTION OF PROPOSAL

LIST OF HOMEOWNERSHIP COUNSELORS (REGULATION X - § 1024.20)

The proposal would amend Regulation X to require lenders to provide an applicant for a federally related mortgage loan[1] with a clear and conspicuous list of five homeownership counselors or counseling organizations. As proposed, the required list must include only counselors included in the CFPB's or HUD's most current list. The required list would need to include: (1) five counselors/organizations located in the applicant's zip code (or the closest available); (2) each counselor's/organization's name, address, phone number, and any other contact information available from the CFPB or HUD; and (3) contact information for the CFPB and HUD. To facilitate compliance with the proposed list requirement, the CFPB plans to develop a website portal that will allow lenders to enter the applicant's zip code to generate the required list.

As proposed, the lender must provide the list no later than three business days after the lender, mortgage broker, or dealer receives the loan application; a mortgage broker or dealer may provide the list to the applicant. Where a mortgage broker or dealer provides the list, the lender is not required to provide an additional list but remains responsible for ensuring the list has been provided. The applicant may consent to receive the list electronically.

REQUIREMENTS FOR HIGH-COST HOME MORTGAGES (REGULATION Z - § 1026.32)

Coverage

Previously, the statutory protections for HOEPA loans were generally limited to closed-end refinancings and home-equity mortgage loans. The proposal extends the statutory protections for high-cost mortgages to

[1] The proposed list requirement would not apply to applicants for Home Equity Conversion Mortgages.

residential mortgage transactions, such as purchase money mortgage loans, and to open-end credit plans secured by the consumer's principal dwelling (i.e., home-equity lines of credit).

Accordingly, the proposal defines "high-cost mortgage" to mean any consumer credit transaction, other than a reverse mortgage transaction as defined in § 1026.33(a), that is secured by the consumer's principal dwelling and in which any one of the prescribed thresholds is met. The proposed commentary clarifies that a high-cost mortgage includes both a closed-end mortgage loan and an open-end credit plan secured by the consumer's principal dwelling. In particular, the comment further clarifies that with regard to determining coverage under § 1026.32, an open-end transaction is the account opening of an open-end credit plan. Under the proposal, an individual advance of funds or a draw on the credit line under an open-end credit plan subsequent to account opening does not constitute a "transaction."

Threshold Triggers

Prior to enactment of the Dodd-Frank Act, HOEPA coverage was triggered when a loan's annual percentage rate (APR) or its points and fees exceeded certain thresholds as prescribed by TILA and currently implemented by current § 1026.32(a)(1). The Dodd-Frank Act adjusted the two existing thresholds and added a third threshold based on the inclusion of certain prepayment penalties.

The proposal would revise the existing APR and points and fees thresholds in proposed § 1026.32(a)(1)(i) and (ii) and to add the new prepayment penalty threshold in proposed § 1026.32(a)(1)(iii). The CFPB is proposing two alternatives to implement the APR threshold for a high-cost mortgage under amended TILA. Under the proposal, the revised thresholds would generally provide that a consumer credit transaction is a high-cost mortgage if:

- The APR, under Alternative 1, or the Transaction Coverage Rate (TCR), under Alternative 2, at consummation of the transaction exceeds the average prime offer rate (APOR) for a comparable transaction by (1) more than 6.5 percentage points for transactions secured by a first mortgage on the consumer's principal dwelling or 8.5 percentage points, if the dwelling is personal property and the total transaction amount is less than $50,000; or (2) 8.5 percentage points for transactions secured by a subordinate mortgage on the consumer's principal dwelling;
- The total points and fees payable in connection with the transaction, other than bona fide third party charges not retained by the mortgage originator, creditor, or an affiliate of either, exceed: (1) in the case of a transaction for $20,000 or more, 5% of the total transaction amount; or (2) in the case of a loan for less than $20,000, the lesser of 8% of the total transaction amount or $1,000 (adjusted for inflation); or
- The transaction provides for prepayment fees and penalties that (1) may be imposed more than 36 months after consummation or account opening or (2) exceed, in the aggregate, more than 2% of the amount prepaid.

As discussed further below, the CFPB is proposing Alternative 2 in connection with its proposal to simplify and broaden the general definition of finance charge under Regulation Z. The CFPB would not adopt Alternative 2 if it does not change the definition of finance charge. Because the proposal to broaden the definition of finance charge does not apply to open-end transactions, the CFPB proposes to retain the APR as the rate that will be compared to the APOR to determine whether an open-end credit plan is a high-cost mortgage under HOEPA.

Potential Expansion of the Definition of Finance Charge

Alternative 2 would account for the changes in the calculation of the finance charge (and thus APR) that the CFPB is separately considering in its TILA-RESPA proposal. Under that proposal, creditors would use a simpler, more inclusive definition of the finance charge for closed-end credit secured by real property or a dwelling, which is in turn used to compute the APR that is disclosed to consumers. As discussed in that proposal, the CFPB believes that the expanded definition could have significant benefits to consumers by making the APR a more useful and accurate tool for comparing the overall cost of credit. At the same time, the proposal could benefit creditors by reducing compliance burden and litigation risk because the finance charge calculation would be easier to perform. However, the CFPB recognizes that a more inclusive definition of the finance charge could expand the coverage of HOEPA because closed-end mortgage loans would have higher APRs, which would result in some additional loans being covered as high-cost mortgages.[2]

Currently, TILA and Regulation Z permit creditors to exclude several fees or charges from the finance charge, including most fees or charges imposed by third parties. The Federal Reserve Board had proposed expanding the definition of finance charge in its 2009 Closed-End proposal and the CFPB has after careful consideration decided to propose a similar change. Specifically, the TILA-RESPA proposal would maintain TILA's definition of a finance charge as a fee or charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor. However, the proposal would require the finance charge to include additional creditor charges and most charges by third parties. The CFPB is proposing a revised definition of the finance charge because the CFPB believes that the simpler finance charge could effectuate the purposes of TILA and facilitate compliance by enhancing consumer understanding and reducing compliance costs.

However, one effect of the expansion of the definition of finance charge would be to expand the number of loans exceeding HOEPA's APR trigger and other statutory and regulatory provisions that incorporate an APR threshold for coverage. There are currently some differences between the APR and the APOR, which is the benchmark rate under the Dodd-Frank Act for determining HOEPA coverage. The APOR is generally calculated using data that includes only contract interest rate and points, but not other origination fees. The current APR includes not only discount points and origination fees but also other charges the creditor retains and certain third-party charges. The proposed simpler, more inclusive finance charge, which would also include most third-party charges, would widen the disparity between the APR and the APOR and expand coverage of HOEPA.

In conjunction with its efforts to quantify the effect of an expanded definition of finance charge, the CFPB is weighing whether modifications may be warranted to approximate coverage levels under the current definition. It is not clear from the legislative history of the Dodd-Frank Act whether Congress was aware of the Board's 2009 Closed-End Proposal to expand the current definition of finance charge or whether Congress considered the interplay between an expanded definition and coverage under the high-cost mortgage provision. In light of this fact and the concerns raised by commenters on the Board's 2009 Closed-End Proposal regarding effects on access to credit, the CFPB believes that it is appropriate to explore alternatives to implementation of the expanded finance charge definition for purposes of HOEPA coverage.

<u>Transaction Coverage Rate (TCR):</u> As discussed above, an alternative method of compensating for the broader definition of finance charge would be to replace the APR benchmark for closed-end mortgage loans with the TCR. The CFPB has proposed this as Alternative 2 for proposed § 1026.32(a)(1)(i), for substantially the same reasons that the Board proposed adopting the TCR to address the impact of the expanded definition of finance charge upon other regulatory triggers. Specifically, the TCR would be defined as the rate used to determine whether a closed-end mortgage loan is a high-cost mortgage subject to § 1026.32. The TCR would be determined in accordance with the applicable rules of Regulation Z for the calculation of the APR for a closed-end transaction, except that the prepaid finance charge would include only charges that will be retained by the creditor, a mortgage broker, or any affiliate of either.

The TCR would not reflect certain costs paid to third parties that would be disclosed to consumers as part of the finance charge under the current and proposed definitions. For example, the current finance charge reflects mandatory credit life insurance, and the proposed more inclusive finance charge would reflect such additional third-party charges as title insurance premiums. However, the TCR would not include either amount. Thus, the TCR might result in some loans not being classified as high-cost mortgages that would otherwise qualify under an APR threshold.

The CFPB expects that, relative to current rules, the TCR would remove from HOEPA coverage fewer overall transactions than the expanded finance charge would add. Thus, the CFPB believes that the TCR may maintain the primary benefits of HOEPA while also offering other significant benefits, such as: (1) the CFPB believes that the TCR would be easier to calculate than the current APR, and could therefore result in reduced compliance burden and litigation costs for creditors; and (2) the TCR has been proposed in two prior proposals of the Board relating to higher-priced mortgage loans.

[2] The revised definition would also affect calculation of HOEPA's threshold based on points and fees.

Furthermore, the CFPB has authority to provide additional requirements, classifications, differentiations, or other provisions, and to provide for such adjustments and exceptions for all or any class of transactions as are necessary, in the CFPB's judgment, to effectuate the purposes of TILA and facilitate compliance. The CFPB understands that most lenders currently do not make HOEPA loans, and previous comments received on the Board's proposal suggest that some lenders may cease making loans that are defined as high-cost mortgages solely as a result of the proposed more inclusive finance charge. The CFPB is therefore evaluating whether the proposed use of the TCR could maintain the special protections for consumers of high-cost mortgages while ensuring that the effects of a more inclusive finance charge would not restrict the availability of credit. In addition, the CFPB believes that the proposal to use the TCR would facilitate compliance by substituting a simpler calculation for the finance charge for purposes of determining whether a transaction is a high-cost mortgage. Creditors would therefore have more certainty about the calculation for purposes of determining coverage of closed-end mortgage loans. Therefore, the CFPB believes that the proposed adjustment may effectuate the purposes of TILA, as amended by HOEPA, and facilitate compliance without undermining consumer protections against abusive practices, the availability of credit, or the interest of the borrowing public.

Determination of Transaction Coverage Rate or Annual Percentage Rate

TILA specifies the interest rate used to determine the APR for purposes of the APR threshold. TILA requires that: (1) in connection with a fixed-rate transaction, the APR must be based on the interest rate in effect on the date of consummation; (2) in connection with a transaction with a rate that varies solely in accordance with an index, the APR must be based on the interest rate determined by adding the maximum margin permitted at any time during the loan agreement to the index rate in effect on the date of consummation; and (3) in connection with any other transaction in which the rate may vary at any time during the term of the loan for any reason, the APR must be based on the maximum interest rate that may be charged during the term of the loan.

Under the proposal, for purposes of the APR trigger, the calculation of the transaction coverage rate or APR, as applicable, for a fixed-rate transaction would need to be based on the interest rate in effect on the date of consummation or account opening. The proposal would require that for a variable-rate transaction in which the interest rate may vary during the term of the loan or plan in accordance with an index outside the creditor's control, the transaction coverage rate or APR, as applicable, must be based on an interest rate that is determined by adding the maximum margin permitted at any time during the term of the loan or plan to the index rate in effect on the date of consummation or account opening. In addition, the proposal would require that for a loan in which the interest rate may vary during the term of the loan the TCR or APR, as applicable, must be based on the maximum interest rate that may be imposed during the term of the loan.

PROHIBITED ACTS OR PRACTICES IN CONNECTION WITH HIGH-COST MORTGAGES (REGULATION Z - §1026.34)

Repayment Ability for High-Cost Mortgages

Under the proposal, § 1026.34(a)(4)(iii) would be amended to clarify the criteria that a creditor must satisfy in order to obtain a presumption of compliance with the repayment ability requirements for high-cost mortgages that are open-end credit plans. Currently, a creditor must determine the consumer's repayment ability using the largest payment of principal and interest scheduled in the first seven years following consummation and taking into account current obligations and mortgage-related obligations. The proposal would require a creditor to determine the consumer's repayment ability taking into account current obligations and mortgage-related obligations, and using the largest required minimum periodic payment. Furthermore, the proposal would require a creditor to determine the largest required minimum periodic payment based on the following assumptions: (1) the consumer borrows the full credit line at account opening with no additional extensions of credit; (2) the consumer makes only required minimum periodic payments during the draw period and any repayment period; and (3) the maximum APR that may apply under the payment plan applies to the plan at account opening and will apply during the draw period and any repayment period.

Pre-Loan Counseling

The proposal would implement a counseling requirement for high-cost mortgages, which provides that a creditor shall not extend a high-cost mortgage unless the creditor receives written certification that the consumer has obtained counseling on the advisability of the mortgage from a HUD-approved counselor. As proposed, the required counseling must occur after the consumer receives either the good faith estimate required under RESPA, or the disclosures required for open-end credit. The high-cost mortgage disclosure is generally required to be provided to the consumer no later than three business days prior to consummation of the loan, and one of the disclosures required under RESPA, the HUD-1, currently may be provided to the consumer at settlement.

Under the proposal, a creditor would be required to provide a consumer for whom counseling is required, with a notice containing the website addresses and telephone numbers of the CFPB and HUD for access to information about housing counseling, and a list of five counselors/organizations approved by HUD to provide high-cost mortgage counseling.

As discussed above regarding Regulation X, the CFPB is proposing that creditors will be required to provide a list of homeownership counselors to mortgage loan applicants generally. In order to facilitate compliance, the CFPB is proposing a safe harbor that provides that a creditor will be deemed to have complied with the requirements of this section regarding pre-loan counseling if the creditor provides the list of homeownership counselors/organizations to a consumer for whom high-cost mortgage counseling is required.

Other Proposed Changes (to § 1026.34)

Modification and Deferral Fees: The CFPB is proposing a new § 1026.34(a)(7) to implement the prohibition on modification and deferral fees for high-cost mortgages in new section 129(s) of TILA, as added by section 1433(b) of the Dodd-Frank Act. As proposed, § 1026.34(a)(7) closely follows the statutory language in its implementation of section 129(s).

Late Fees: Section 1433(a) of the Dodd-Frank Act added to TILA a new section 129(k) establishing limitations on late fees on high-cost mortgages. The proposal implements these limitations, with minor modifications for clarity, in proposed § 1026.34(a)(8).

Payoff Statements: The CFPB is proposing a new § 1026.34(a)(9) to implement new section 129(t) of TILA, added by section 1433(d) of the Dodd-Frank Act, which: (1) specifically prohibits, with certain exceptions, a creditor or servicer from charging a fee for “informing or transmitting to any person the balance due to pay off the outstanding balance on a high-cost mortgage”; and (2) requires payoff balances for high-cost mortgages to be provided within five business days of a request by a consumer or a person authorized by the consumer to obtain such information.

Financing of Points and Fees: Section 1433 of the Dodd-Frank Act added to TILA a new section 129(m) prohibiting the direct or indirect financing of (1) any points and fees; and (2) any prepayment penalty payable by the consumer in a refinancing transaction if the creditor or an affiliate of the creditor is the holder of the note being refinanced. The CFPB implements new TILA section 129(m) in proposed § 1026.34(a)(10). Proposed § 1026.34(a)(10) implements all aspects of the statute, except that the CFPB omits from the proposal statutory language concerning the financing of prepayment penalties payable by the consumer in a refinancing transaction. The CFPB notes that such penalties are subsumed in the definition of points and fees for § 1026.32 in proposed § 1026.32(b)(1)(vi) and (3)(iv).

EFFECTIVE DATE

The CFPB’s proposal seeks comment on when a final rule should be effective. Because the final rule will provide important benefits to consumers, the CFPB seeks to make it effective as soon as possible. However, the CFPB understands that the final rule will require lenders and brokers to make systems changes and to retrain their staff. In addition, industry will at approximately the same time be implementing a number of other changes relating to other Dodd-Frank Act provisions, some of which will take effect within one year after issuance of final implementing rules. Therefore, the CFPB is seeking comment on how much time industry needs to make these changes.

QUESTIONS TO CONSIDER REGARDING THE PROPOSAL

1) The CFPB seeks comments on the costs and benefits of the provision of the list of homeownership counselors to consumers who are applicants for refinances and home-equity lines of credit. The CFPB also

seeks comments on the potential effect of its proposal on access to homeownership counseling generally by consumers, and the effect of increased consumer demand for counseling on existing counseling resources. Including comments on the effect on counseling resources of providing the list beyond applicants for purchase money mortgages.

2) Should the CFPB adopt certain adjustments or accommodations in its HOEPA implementing regulations if it adopts a broader definition of "finance charge" under Regulation Z? That change, which the CFPB is proposing in connection with its proposal to integrate mortgage disclosures, would otherwise cause more loans to exceed the APR and points and fees triggers and be classified as high-cost mortgages under HOEPA.

3) The CFPB seeks comments on whether, if it adopts the broader definition of finance charge in the TILA-RESPA rulemaking, it should compensate for that change to approximately offset the impact of a broader definition of finance charge on HOEPA coverage levels.

4) Dodd-Frank amends TILA to allow a creditor or assignee of a high-cost mortgage in certain circumstances to correct a failure to comply, when acting in good faith, with HOEPA requirements. However, the CFPB is currently not proposing to issue regulatory guidance concerning this provision. To what extent are creditors or assignees likely to invoke this provision? Would regulatory guidance be useful? If so, what issues would be most important to address?

5) The CFPB seeks comments on its proposed rules for determining the APR for HOEPA coverage, including on whether any aspect of the proposal could result in unwarranted, over-inclusive HOEPA coverage of HELOCs.

6) The CFPB requests comments on the proposed definition of points and fees for open-end credit plans, including on whether any additional fees should be included in the definition. In particular, the CFPB requests comment on whether compensation paid to originators should be included in the calculation of points and fees from open-end credit plans.

7) The CFPB is seeking comments on an appropriate implementation period for the final rules.

8) Any other comments or questions.