Summary of 2013 Mortgage Rules Issued by the Consumer Financial Protection Bureau

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Executive Summary

The Consumer Financial Protection Bureau between January 10, 2013, and January 20, 2013, issued eight final rules relating to residential mortgages:

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These rules will fundamentally reshape the origination, servicing, and securitization of residential mortgages in the United States. All participants in the mortgage market — consumers, lenders, securitizers, servicers, and investors, among others — will feel the influence of the new rules.

Companies must address how to meet the operational challenges they face over the next year in building the systems, policies and procedures, controls, and business practices that comply with the new requirements. We believe there are three key challenges mortgage-market participants must navigate during the next year:

(1) Strategic reassessment of the mortgage business: Industry participants must determine the impact of the new rules on current business practices and make strategic decisions about how to conduct their businesses going forward. Mortgage lenders should consider, among other things, product design and offerings, pricing strategies, underwriting standards, compensation practices, whether to bring functions in-house or outsource to third parties, and possible risks related to fair lending and the Community Reinvestment Act. Mortgage servicers should consider, among other things, pricing strategies, loss-mitigation and foreclosure procedures, staffing needs, and training.

(2) Project planning and management: The volume and scope of the new rules and the one-year implementation deadline pose significant planning and management challenges. Because the rules impact virtually every aspect of a mortgage business, coordination among different units within the organization will be critical to achieving timely compliance. Success will require, among other things, revising business practices and related policies and procedures, developing new systems requirements, updating and testing systems changes, conducting staff training, and revising compliance-testing plans.

(3) Unknown variables: A number of unknown factors compound the other implementation challenges mortgage market participants face. The CFPB has promised to provide additional interpretive guidance this spring and to issue readiness guides this summer. Examination procedures are not expected until later this year. Given the time constraints, awaiting further guidance before moving forward with implementation is not an attractive option. How other mortgage-market participants choose to respond to the new rules is another unknown factor of significance. Finally, it is not known at this time when other proposed mortgage rules from the CFPB and the other regulators will be issued in final form and the impact those rules may have.

Key Issues for Mortgage Origination

We believe that the following are among the most critical issues facing mortgage lenders:

- **Adopt appropriate underwriting standards.** To meet the ability-to-repay requirement, creditors have flexibility to develop their own underwriting standards, but are strongly advised to:
  - Adopt conservative underwriting standards;
  - Validate the standards;
  - Apply the standards consistently; and
  - Periodically revalidate the standards and adjust if necessary.

- **Understand and properly apply the qualified mortgage (QM) criteria.** For a loan to be a "qualified mortgage" (QM), which reduces risk to the creditor, the loan must satisfy certain limits on terms and conditions, pricing, and, in most cases, a maximum debt-to-income ("DTI") ratio. Designing products to meet the QM standards and ensuring correct calculations are made for individual loans are key challenges for creditors.

- **Determine how to stay within the points and fees cap for qualified mortgages.** For a loan to be a QM, total points and fees may not exceed 3% of the total loan amount for most mortgage loans. Keeping points and fees below this cap may require creditors to consider revising their business practices to reduce or eliminate:
  - Mortgage-broker originations;
  - Loan-originator compensation that is attributable to a specific transaction;
  - Real-estate related services obtained from affiliates; and
  - Credit insurance premiums payable at or before consummation, debt cancellation or suspension agreements, and prepayment penalties.

- **Manage fair lending and CRA risk.** Creditors should actively manage the fair lending and CRA risks associated with implementing the ability-to-repay rules. Creditors should assess the potential impact on protected classes of offering only QM loans. Creditors that offer non-QM loans should assess the circumstances under which they will offer such loans and ensure that their underwriting standards are validated and applied consistently.

- **Review loan originator compensation structures.** Loan originators may not be compensated based on a term of the transaction or a proxy for a term of a transaction. Special rules apply to contributions retirement plan and profit-sharing plans.

Key Issues for Mortgage Servicing

We believe that the following are among the most critical issues facing mortgage servicers:

- **Manage transfers of servicing rights.** As mortgage-market participants reevaluate their operations, some firms may exit, and others may expand, their mortgage-servicing operations. The CFPB has announced that, for significant servicing transfers, it will expect the submission of informational plans describing how the risks to consumers will be managed. Thus, firms contemplating the purchase or sale of servicing portfolios before the new rules take effect should prepare for heightened scrutiny of those transfers.

- **Adopt the new dual-tracking restrictions.** New restrictions on pursuing foreclosure at the same time that a loss-mitigation application is pending will require servicers to improve information-management practices and foster cooperation and information sharing between loss-mitigation and foreclosure personnel.

- **Revise business practices to implement the new loss-mitigation procedures.** New procedures for evaluating loss-mitigation applications include numerous, time-sensitive benchmarks. Servicers need to revise business practices, improve information-management practices, upgrade systems, develop a number of new highly customizable disclosures without the benefit of model forms, establish an appeals process, and ensure they have sufficient numbers of well-trained staff to comply with these new requirements. All this must be implemented against a backdrop of differing investor requirements for loss mitigation. In addition, servicers should consider structuring loss-mitigation processes to elicit loss-mitigation applications from borrowers as early as possible to avoid last-minute delays in foreclosures.

We hope that you find this overview and our accompanying summary of the rules helpful as you prepare for the new regulatory requirements.

Ability-to-Repay and Qualified Mortgage Standards

Effective date: January 10, 2014

I. Overview

The final rule generally requires creditors to make a reasonable, good-faith determination at or before consummation of a consumer credit transaction secured by a dwelling that a consumer will have a reasonable ability to repay the loan according to its terms. The ability-to-repay provisions do not apply to home equity lines of credit, mortgages secured by a consumer's interest in a timeshare plan, reverse mortgages, temporary or "bridge" loans of 12 months or less, or the construction phase of 12 months or less of a construction-to-permanent loan. The rule also establishes certain protections from liability in the form of a safe harbor for prime "qualified mortgages" and a rebuttable presumption for subprime "qualified mortgages." The term "qualified mortgage" is discussed in detail below.

The final rule also limits the application of prepayment penalties to any consumer credit transaction secured by a dwelling. The prepayment penalty limitations do not apply to a home equity line of credit or a mortgage secured by a consumer's interest in a timeshare plan. A prepayment penalty is permitted only if it is otherwise permitted by law and the transaction is one in which the annual percentage rate (APR) cannot increase after consummation, the mortgage is a "qualified mortgage," and the mortgage is not a subprime mortgage on the consumer's principal dwelling.

Even when permitted, a prepayment penalty must not apply after the three-year period following consummation and must not exceed 2% of the outstanding loan balance prepaid during the first two years or 1% of the outstanding loan balance prepaid during the third year after consummation. In addition, if the creditor offers the consumer a covered mortgage with a prepayment penalty, it must offer an alternative covered mortgage without a prepayment penalty that meets certain conditions to qualify as an alternative. Finally, if covered mortgages with prepayment penalties are offered through a mortgage broker or by an intended assignee, certain conditions apply.

The final rule requires creditors to retain evidence of compliance with the ability to repay and prepayment penalty provisions for three years after a covered mortgage is consummated.

Contemporaneous with the January 10, 2013 final rule, the CFPB issued a proposal with some exemptions, modifications, and clarifications to the ability-to-repay requirements. On May 29, 2013, the CFPB adopted a final rule that provided additional exemptions, created a fourth way that a mortgage could become a qualified mortgage, broadened the loans made by small creditors that fall within the qualified-mortgage safe harbor, and excluded from the points and fees calculation some compensation for loan originators. On May 2, 2013, the CFPB proposed certain revisions to the mortgage-servicing and ability-to-repay/qualified-mortgage rules.

II. Ability-to-repay provisions

A. Scope.

The ability-to-repay provisions are applicable to any consumer credit transaction secured by a dwelling, except for home equity lines of credit, mortgages secured by a consumer's interest in a timeshare plan, reverse mortgages, temporary or “bridge” loans of 12 months or less, or the construction phase of 12 months or less of a construction-to-permanent loan.

The May 29, 2013 final rule exempted from the ability-to-repay requirements creditors designated as: (a) a Community Development Financial Institution by the U.S. Department of the Treasury; (b) a Community Housing Development Organization by the U.S. Department of Housing and Urban Development (“HUD”) that is participating in various HUD programs; and (c) a nonprofit organization under the Internal Revenue Code that makes a limited number of loans, and extends credit only to low-to-moderate income consumers. The final rule also exempted loans made under the Department of Treasury’s Hardest Hit Fund.

B. Determination of repayment ability.

Before making a mortgage loan, a creditor must make a reasonable and good-faith determination, at or before consummation, of a consumer's ability to repay the loan according to its terms. Whether a particular determination is reasonable and in good faith depends upon the creditor’s underwriting standards, the facts and circumstances of the particular credit extension, and the creditor’s application of its underwriting standards to those facts and circumstances.

1. **Evidence of good faith determination** may include:
    - **a.** Consumer actually makes timely payments for significant period of time;
    - **b.** Use of underwriting standards that historically resulted in low rates of delinquency and default during adverse economic conditions;
    - **c.** Use of underwriting standards based on empirically derived, demonstrably and statistically sound models.
2. **Evidence of a lack of a good faith determination** may include:
    - **a.** Default shortly after consummation (or, for an adjustable-rate, interest-only, or negative amortization mortgage, default shortly after the expiration of the period when introductory fixed-interest-rate, interest-only, or negatively amortizing payments are permitted);
    - **b.** Use of underwriting standards that have historically resulted in high rates of delinquency and default during adverse economic conditions;
    - **c.** Inconsistent application of underwriting standards without reasonable justification;
    - **d.** Disregarding evidence of ineffectiveness of underwriting standards in determining consumers’ ability to repay;
    - **e.** Disregarding evidence of insufficient income to cover other expenses;
    - **f.** Disregarding evidence that consumer would be able to pay only if he/she subsequently were to refinance or sell the property.

C. Basis for determination.

When determining a consumer’s ability to repay, the final rule requires a creditor to consider the following eight underwriting factors:

1. Current or reasonably expected income or assets (except for the value of the dwelling that secures the loan);
2. Current employment status;
3. The monthly payment on the loan using (1) the greater of the fully indexed rate or introductory interest rate, and (2) monthly, fully amortizing, and substantially equal payments. Special calculation rules apply to loans with a balloon payment, interest-only loans, and negative-amortization loans;[1]
4. The monthly payment on any simultaneous loans to the same consumer and secured by the same dwelling that the creditor knows or has reason to know will be or has been made at or before consummation. The creditor must make this calculation using the same criteria currently under discussion if the loan is subject to the ability-to-repay rules and, for a home equity line of credit, using the periodic payment required and the amount of credit to be drawn at or before the loan covered by this provision is consummated;
5. The monthly payment for property taxes, premiums, and similar charges for insurance and debt cancellation required by the creditor; fees and special assessments (if paid on a recurring basis) imposed by a condominium, cooperative, or homeowners association; ground rent; and leasehold payments;
6. Current debt obligations, alimony, and child support;
7. The monthly debt-to-income ratio or residual income (see Appendix Q for a summary of the final rule's guidance on monthly debt-to-income ratio calculations). For the debt-to-income ratio, the creditor must consider the ratio of the consumer's total monthly debt obligations to the consumer's total monthly income. For the residual income calculation, the creditor must consider the consumer's remaining income after subtracting the total monthly debt obligations from the total monthly income; and
8. Credit history, which may but need not include a credit report, credit score, or nontraditional credit references, such as rental payment history or utility payments.

Aside from certain standard calculation methodologies described above and in Appendix Q below, the final rules do not prescribe comprehensive underwriting standards that creditors must use. Creditors are free to develop their own underwriting standards and change those standards over time in response to empirical information and changing economic and other conditions. Creditors may, but are not required to, look to guidance issued by the Federal Housing Administration, the Department of Veteran's Affairs, the Department of Agriculture, or Fannie Mae or Freddie Mac while operating under conservatorship of the Federal Housing Finance Agency, in establishing their underwriting standards.

[1] For loans with a balloon payment, the creditor must use: (1) the maximum payment scheduled during the first five years after the date on which the first regular periodic payment will be due for a loan that is not a higher-priced transaction; or (2) the maximum payment in the payment schedule for a higher-priced covered transaction. For interest-only or negative amortization loans, the creditor must use: (1) the greater of the fully indexed rate or any introductory interest rate; and (2) substantially equal, monthly payments of principal and interest that will repay the loan amount over the term of the loan remaining as of the date the loan is recast.

D. Verification using third-party records.

The final rule requires creditors to verify the information they rely upon in making their ability-to-repay determinations using reasonably reliable third-party records.

1. **Income or assets.** A creditor must verify the amounts of income or assets relied upon in making its determination using third-party records that provide reasonably reliable evidence of the consumer's income or assets. Acceptable records include tax-return transcripts issued by the IRS, copies of tax returns filed by the consumer, IRS form W-2s or similar forms, payroll statements, records from a financial institution, records from the consumer's employer, records from a government agency for income from benefits or entitlements, or receipts from the consumer's use of check-cashing or fund-transfer services.
2. **Employment status.** A creditor may verify a consumer's employment status orally, but must prepare a record of the information obtained orally. For military personnel, a creditor may rely on a military Leave and Earnings Statement or the Department of Defense electronic database of consumers protected by the Servicemembers Civil Relief Act.
3. **Credit report.** A credit report generally is considered a reasonably reliable third-party record for items customarily found on a credit report. A credit report is not a reasonably reliable third-party record for debt obligations not customarily found on the report, such as alimony and child-support obligations. Inaccurate or disputed information on a credit report may be disregarded without obtaining additional verifying records. If a credit application lists a current debt not shown on the credit report, the creditor may consider the debt without further verification.

E. Exception for refinancing certain types of mortgages into a "standard" mortgage.

The refinancing of an interest-only or negative amortization ARM loan with an introductory fixed interest rate of one year or longer (a "nonstandard" mortgage) into a "standard" mortgage is exempt from the ability-to-repay requirements if certain conditions are met.

A "standard" mortgage is a mortgage that:

- Provides for regular periodic payments and does not cause the principal balance to increase, allow the consumer to defer repayment of principal, or result in a balloon payment;
- Satisfies the points and fees cap applicable to a qualified mortgage;
- Has a term of not more than 40 years;
- Has a fixed interest rate for at least the first five years after consummation, and for which the proceeds are used solely to pay off the non-standard mortgage and RESPA-disclosed closing and settlement charges.

The exemption applies if: (1) the creditor for the standard mortgage is the holder or servicer of the current non-standard mortgage; (2) the monthly payment for the standard mortgage is materially lower than the monthly payment for the non-standard mortgage; (3) the creditor receives the consumer's application for the standard mortgage no later than two months after the non-standard mortgage has been recast;[2] (4) the consumer has had no more than one 30-day late payment during the past 12 months; (5) the consumer has made no payments more than 30 days late during the past six months; (6) the non-standard mortgage was made in compliance with the ability-to-repay rules once they become effective; and (7) the creditor has considered whether the standard mortgage likely will prevent a default by the consumer.

III. Qualified-mortgage provisions

A. Definition of "qualified mortgage"

A "qualified mortgage" is a mortgage that meets any one of several definitions set forth below. For qualified mortgages, the creditor or assignee enjoys certain legal protections in the form of a safe harbor or rebuttable presumption of compliance with the ability-to-repay requirements, as discussed below in III.B.

1. **Standard definition.** A qualified mortgage is a mortgage subject to the ability-to-repay requirements that meets the following criteria:

   a. The loan provides for regular, substantially equal, periodic payments (allowing for payments changes on ARMs or step-rates) and does not result in negative amortization, allow the consumer to defer repayment of principal (subject to a limited exception), or result in balloon payments (subject to a limited exception);

   b. The loan term does not exceed 30 years;

   c. Total points and fees do not exceed (loan amounts and dollar thresholds indexed for inflation):

      - Loans $100,000 and greater: 3% of total loan amount;
      - Loans $60,000 and greater but less than $100,000: $3,000;
      - Loans $20,000 and greater but less than $60,000: 5% of total loan amount;
      - Loans $12,500 and greater but less than $20,000: $1,000;
      - Loans less than $12,500: 8% of total loan amount.

      (For a discussion of the calculation of points and fees, see the Points and Fees Supplement below.)

   d. The creditor underwrites the loan, taking into account the monthly payment for mortgage-related obligations, using:

      - The maximum rate that may apply during the first five years of the loan; and
      - Periodic payments of principal and interest that will repay either the outstanding balance over the remaining term of the loan as of date the interest rate adjusts to the maximum rate, or the loan amount over the term.

[2] A "recast" means the end of the period during which payments on an interest-only or negatively amortizing basis are permitted for interest-only or negative amortization loans, or the end of the period during with payments at an introductory fixed rate are permitted under an adjustable-rate mortgage.

e. Creditor considers and verifies current and expected income and assets, debt obligations, alimony, and child support.

f. The consumer's total or "back-end" debt-to-income ratio at consummation does not exceed 43%, calculated in accordance with Appendix Q.

2. **Temporary alternative definition.** For a temporary period of time, a qualified mortgage also is a mortgage subject to the ability-to-repay requirements that meets the following criteria:

   a. The loan is <u>eligible</u> to be:

      - Purchased or guaranteed by Fannie Mae or Freddie Mac operating under conservatorship or receivership by FHFA (or limited-life successor regulatory entity);
      - Insured by HUD/FHA or the Rural Housing Service; or
      - Guaranteed by the VA or U.S. Dept. Agriculture;

   b. A loan provides for regular, substantially equal, periodic payments (allowing for payment changes on ARMs or step-rates) and does not result in negative amortization, allow the consumer to defer repayment of principal (subject to a limited exception), or result in a balloon payments (subject to a limited exception);

   c. The loan term does not exceed 30 years; and

   d. Total points and fees do not exceed the limits under the standard definition.

   Under the alternative, there is no maximum debt-to-income ratio. This temporary rule will sunset on January 10, 2021, or in accordance with rules adopted by the respective agencies, whichever occurs first.

   On May 2, 2013, the CFPB proposed certain clarifications to the temporary standard. One would provide that a creditor determining loan eligibility can rely on written agreements with Fannie Mae or Freddie Mac ("GSEs") that specify permitted variations from the GSEs' automated underwriting systems and written guides. Another would exempt creditors from meeting GSE or agency standards wholly unrelated to assessing a consumer's ability to repay, such as requirements relating to selling, securitizing, or delivering consummated loans. Finally, the proposal would clarify that a loan subject to a repurchase or indemnification demand by a GSE or agency may still be a qualified mortgage, and a loan's status as a qualified mortgage is generally determined by eligibility at the time of origination.

3. **Definition of a qualified mortgage for balloon loans by small, rural creditors.** Qualified mortgages include certain mortgages with balloon payment features made by small, rural creditors. Creditors are only eligible to make balloon-payment qualified mortgages if they originate at least 50% of their first-lien mortgages in counties that are rural or underserved, have less than $2 billion in assets, and (along with their affiliates) originate no more than 500 first-lien mortgages per year. Creditors must generally hold the loans on their portfolios for three years in order to maintain their qualified-mortgage status. The bureau will designate a list of "rural" and "underserved" counties each year. In addition, such loans must meet the following criteria to be qualified mortgages:

a. Fixed-rate loans with scheduled payments that are substantially equal, using an amortization period of not more than 30 years;

b. No negative amortization;

c. Loan term greater than five years but not more than 30 years;

d. Points and fees limited to the same extent as in other qualified mortgages;

e. Verification of income/assets, debt, alimony, and child support;

f. Determination at or before consummation that the consumer can make scheduled payments, plus payments for all mortgage-related obligations from current/reasonably expected income/assets; and

g. Consideration of debt-to-income ratio or residual income.

4. **Definition of a qualified mortgage for small creditor portfolio loans.** The May 29, 2013 final rule adopted a fourth definition of a qualified mortgage applicable to loans made by creditors that, together with affiliates, make 500 or fewer loans subject to the ability-to-repay rules during the preceding calendar year and have total assets of less than $2 billion as of the end of the previous calendar year. Loans must still satisfy all of the requirements for a qualified mortgage under the standard definition with the exception of the maximum 43% debt-to-income ratio. Small creditors still must evaluate consumers' debt-to-income ratio or residual income, but the loans need not satisfy a specific debt-to-income ratio. Also, creditors generally must hold these loans in portfolio to retain their qualified mortgage status. Exceptions to the portfolio requirement include sales or transfers three years or more after origination; to another small creditor; pursuant to a capital restoration plan or other agency order; in connection with bankruptcy; and in connection with a merger.

5. **Temporary definition for balloon payment qualified mortgages by small creditors.** The May 29, 2013 final rule provided a temporary definition for qualified mortgages that applies to balloon-payment loans offered by small creditors that do not operate predominantly in rural or underserved areas. This definition applies only to covered transactions completed on or before January 10, 2016, and thus gives small creditors a two-year transition period during which they can treat balloon-payment loans that they hold in portfolio as qualified mortgages.

B. Qualified-mortgage safe harbor and presumption

The final rule provides a "safe harbor" for compliance with the ability-to-repay rules to creditors or assignees of loans that satisfy the definition of a qualified mortgage and are not higher-priced mortgage loans. The final rule also provides a "rebuttable presumption" of compliance with the ability-to-repay rules to creditors or assignees for higher-priced mortgage loans, defined as loans with an APR exceeding the average prime offer rate ("APOR") by 1.5 or more percentage points for first-lien, or by 3.5 or more percentage points for subordinate-lien loans. The line is drawn as a rule of thumb to separate prime loans from subprime loans.

The May 29, 2013 final rule expanded the number of loans made by small creditors that meet the qualified-mortgage safe harbor. Specifically, for loans that are qualified mortgages under the small, rural creditor balloon-loan test or the small-creditor portfolio loan test, the safe harbor applies if the APR on a first-lien mortgage does not exceed the APOR by 3.5 or more percentage points.

1. **Safe harbor.** If a prime loan satisfies the qualified-mortgage criteria described above, it will be conclusively presumed that the creditor made a good-faith and reasonable determination of the consumer's ability to repay. Even under the safe harbor, however, a consumer may challenge a determination that his loan met the criteria for a qualified mortgage.
2. **Rebuttable presumption.** If a subprime loan satisfies the qualified mortgage criteria described above, there is a rebuttable presumption that the creditor made a good-faith and reasonable determination of the consumer's ability to repay. Consumers may rebut the presumption by showing that, at the time the loan was originated, the consumer's income and debt obligations left insufficient residual income to meet living expenses. Factors considered include the consumer's monthly payments on the loan, loan-related obligations, and any simultaneous loans of which the creditor was aware, as well as any recurring, material living expenses of which the creditor was aware at the time of consummation. One example of such recurring expenses is recurring medical expenses of which the creditor was aware at consummation.[3] Guidance accompanying the rule notes that the longer the period of time that the consumer has demonstrated actual ability to repay the loan by making timely payments, without modification or accommodation, after consummation or, for an adjustable-rate mortgage, after recast, the less likely the consumer will be able to rebut the presumption based on insufficient residual income.

IV. Prepayment penalties

The final rule generally prohibits prepayment penalties, unless the prepayment penalty is otherwise permitted by law and the transaction (1) has an annual percentage rate that cannot increase after consummation, (2) is a qualified mortgage, and (3) is not a subprime mortgage on a consumer's principal dwelling.

Even where prepayment penalties are permitted, the final rule imposes the following limits on the terms of such provisions: (1) the prepayment penalty must not apply after three years after consummation; and (2) the prepayment penalty must not exceed 2% of the outstanding loan balance prepaid during the first two years after consummation, or 1% of the outstanding loan balance prepaid during the third year after consummation.

Moreover, a creditor may not offer a consumer a mortgage with a prepayment penalty unless it also offers the consumer an alternative mortgage with no such penalty that meets the following criteria:

- The APR does not increase after consummation;
- The same type of interest rate (e.g., fixed-rate or step-rate) as the interest rate on the mortgage with the prepayment penalty;
- The same loan term as the one on the mortgage with the prepayment penalty;
- The alternative satisfies the qualified-mortgage requirement for regular periodic payments that are substantially equal;

[3] Consideration of recurring medical expenses is problematic insofar as the medical information rules issued under the Fair Credit Reporting Act (Regulation V) prohibit a creditor from considering a consumer's medical health, condition, history, type of treatment, or prognosis in any credit eligibility decision.

- The alternative satisfies the qualified-mortgage limitations on points and fees; and
- The creditor has a good-faith belief that the consumer is likely to qualify for the alternative mortgage without the prepayment penalty.

If the creditor offers a consumer a mortgage with a prepayment penalty through a mortgage broker, the creditor must: (1) present the broker an alternative mortgage without a prepayment penalty; and (2) establish by agreement that the broker must present the consumer with an alternative mortgage without a prepayment-penalty offered by the creditor or another creditor if the other creditor offers a lower interest rate or lower total dollar amount of discount points and origination points or fees.

If the creditor is a loan originator and presents the consumer with a mortgage with a prepayment penalty offered by a person to which the creditor would assign the mortgage, the creditor must present the consumer with an alternative mortgage without a prepayment penalty that is offered by the assignee or another person if the other person offers a lower interest rate or lower total dollar amount of discount points and origination points or fees.

There is no violation if the consumer obtains a mortgage without a prepayment penalty from the creditor or does not obtain a mortgage from the creditor.

V. Record retention

The final rule requires creditors to retain records that evidence compliance with the ability-to-repay and prepayment-penalty provisions for three years after consummation. The rule also prohibits evasion of the rule by structuring a closed-end extension of credit that does not meet the definition of open-end credit as an open-end plan.

VI. Liability for violations

A. Violations of the ability-to-repay provisions can result in regular TILA damages (actual damages, statutory damages of up to $4,000, costs, and attorney's fees) and in enhanced damages for violation of the ability-to-repay requirements (an amount equal to the sum of all finance charges and fees paid by the consumer, unless the creditor demonstrates that the failure to comply is not material).

B. A private right of action may be brought before the end of the three-year period beginning on the date of the occurrence of the violation. However, when a creditor, assignee, or other holder or anyone acting on their behalf initiates a judicial or non-judicial foreclosure, or any other action to collect the debt, a consumer may assert a violation by a creditor of the ability-to-repay requirement as a matter of defense by recoupment or set-off without regard for the time limit described above.

C. The amount of recoupment or set-off shall equal the amount to which the consumer would be entitled as regular and/or enhanced damages (described above) for a valid claim brought in an original action against the creditor, plus the costs to the consumer of the action, including a reasonable attorney's fee. If judgment is rendered after the expiration of the three-year period from the date of violation, the amount of recoupment or set-off shall not exceed three years of finance charges and fees.

D. An action to enforce a violation may also be brought by the appropriate state AGs.

Points and Fees Supplement

I. **Definition.** Points and fees, in connection with a closed-end credit transaction, means the fees or charges listed in II. below that are known at or before consummation.

II. Charges included in points and fees for closed-end credit transactions

- **Finance Charge.** All items included in the finance charge under (§ 1026.4(a) and (b)), unless excluded by III. below. The finance charge generally includes charges payable, directly or indirectly, by the consumer and imposed by the creditor as a condition of the extension of credit, but does not include charges payable in a comparable cash transaction. Finance charges include, without limitation:
    - Third-party charges if use of an outside party is required by the creditor or if a portion of the third-party charge is retained by the creditor (to the extent of retention);
    - Closing-agent charges if the creditor requires the services covered by the charge, requires imposition of the charge, or retains a portion of the charge (to the extent retained);
    - All mortgage-broker fees, including those paid directly to the broker by the borrower and those that are not required or retained by the creditor.
- **Origination compensation.** All compensation paid directly or indirectly by a consumer or a creditor to a loan originator that can be attributable to the transaction at the time the rate is set, unless the compensation is paid (1) by a consumer to a mortgage broker and that payment has already been included in points and fees as part of the finance charge; (2) by a mortgage broker to a loan originator that is an employee of the mortgage broker; or (3) by a creditor to its loan officers. The points and fees calculation does not include long-term performance pay, compensation based on overall quality of loan files, or base salary.
- **Real-estate-related fees.** All real-estate-related fees listed in 1024.4(c)(7) (other than amounts held for future payment of taxes), unless the charge is reasonable, the creditor receives no direct or indirect compensation in connection with the charge, and the charge is not paid to an affiliate of the creditor. Real-estate-related fees include fees for title examination, abstract of title, title insurance, property survey, preparation of loan-related documents, notarization or credit reports, property appraisals or inspections, and amounts required to be paid into escrow or trustee accounts if not included in the finance charge.
- **Credit-insurance premiums.** Any premiums or other charges payable at or before consummation for any credit insurance or other insurance for which the creditor is a beneficiary, or any payment directly or indirectly for any debt cancellation or suspension agreement.

- **Maximum prepayment penalty.** The maximum prepayment penalty that may be charged or collected under the terms of the loan, other than a waived, bona fide third-party charge imposed if prepayment occurs within 36 months.
- **Total prepayment penalty.** The total prepayment penalty incurred by the consumer if the existing mortgage is refinanced with the current holder, a servicer on behalf of the holder, or an affiliate of either.
- **Loan-level pricing adjustments.** Loan-level pricing adjustments by GSEs, while not directly charged to the borrower, are not explicitly excluded from the points-and-fees calculations.

III. Charges excluded from points and fees (closed-end transaction)

The following items included in the finance charge are <u>not</u> included in the points-and-fees calculation:

- Interest or time-price differential.
- Premium or charge for federal or state mortgage insurance or guaranty.
- Private-mortgage-insurance (PMI) premiums or charges if payable after consummation.
- PMI premiums or charges payable at or before consummation, but only to the extent that the amount that does not exceed FHA insurance (even if the loan would not qualify for FHA insurance), and only if the premium or charge is refundable on a pro rata basis and automatically refunded upon satisfaction of the loan.
- Bona fide third-party charges not retained by the creditor, originator, or any affiliate of either, unless otherwise required to be included in the points-and-fees calculation.
- Up to two bona fide discount points[4] paid by the consumer if the rate does not exceed APOR by more than one percentage point, or up to one point if the rate does not exceed APOR by more than two percentage points.
- Up to two discount points on transactions secured by personal property if the interest rate prior to the discount does not exceed the average rate for loans insured under the National Housing Act plus one point (one discount point if the rate does not exceed the average NHA rate plus two points).

[4] A "bona fide discount point" is an amount equal to one percent of the loan amount (closed-end credit) or credit limit (open-end) paid by the consumer that reduces the interest rate based on a calculation consistent with established industry practices.

Appendix Q – Standards for Determining Monthly Debt and Income

Appendix Q establishes standards that creditors must use to calculate the consumer's total monthly debt-to-income ratio (which cannot exceed 43% at the time of consummation) under the standard QM definition. The standards are based on the FHA Handbook and are not used in connection with balloon QMs as described above.

On May 2, 2013, the CFPB proposed a number of revisions to Appendix Q in response to industry concerns that some of the FHA standards, which were designed to be flexible underwriting standards, were not well-suited to function as bright-line regulatory requirements.

I. Consumer eligibility

A. Stability of Income.

1. **Effective income.** Only income that is verifiable, stable, and continuing may be included in calculating the consumer's monthly gross income.
2. **Verifying and analyzing employment history.** A creditor must verify the consumer's employment history for the most recent two full years. A consumer must explain the reasons for gaps in employment that span one or more months and provide evidence that supports such claims. Allowances can be made for seasonal employment if documented.
3. **Analyzing a consumer's employment record.** When analyzing the probability of continued employment, a creditor must examine: (1) the consumer's past employment record, (2) the consumer's qualifications for this position, (3) the consumer's previous training and education, and (4) the employer's confirmation of continued employment. Frequent job changes may be favorable if they are within the same line of work and show continued advancement income or benefits. Thus, income stability takes precedence over job stability. The CFPB has proposed revising this provision to require creditors to examine only the consumer's past employment record and the employer's confirmation of current, ongoing employment status, rather than confirmation of continued employment status. The proposal would eliminate the requirement to consider the probability of continued employment, qualifications, training and education, and the employer's confirmation of continued employment.
4. **Extended absence.** When recently returning to work after an extended absence, a consumer's income may still be considered effective and stable if certain requirements are met.

B. Salary, wage and other forms of income.

1. **Criteria for salary and wage income.** A creditor must determine whether the income level for each consumer who will be obligated for the mortgage debt can be reasonably expected to continue through at least the first three years of the mortgage loan. Income from sources

other than salaries or wages can be considered as effective, when properly verified and documented by the creditor.[5] The CFPB has proposed revising this provision to eliminate the requirement to predict the consumer's future income for three years. Instead, creditors would be allowed to assume that verified salary or wage income can be reasonably expected to continue as long as the employer verifies current employment and income, and does not indicate that employment has been, or is set to be terminated.

2. **Criteria for other forms of income.** Income from sources other than wages and salaries may be considered effective income if the creditor properly verifies, analyzes, and documents any such income to be included in the monthly income calculation. Generally, income may be considered effective provided that it has continued for the past two years and will likely continue in the future. Income that has continued for less than two years may still be considered eligible, provided that the creditor can justify and document in writing the reasons for using the income for qualifying purposes. Other sources of income include: (1) overtime and bonus income, (2) part-time income, (3) income from seasonal employment, (4) income where primary employment is less than a typical 40 hour work week, (5) commission income, (6) employer differential payments, (7) retirement income, (8) Social Security income, and (9) automobile allowances and expense-account payments.
3. **Specific requirements for certain forms of income.**
   - **Overtime and bonus income** – The creditor must establish and document an earnings trend, and if such income shows a continual decline, the creditor must justify and document in writing why it should be included.
   - **Employer differential payments** – The amount of an employer mortgage subsidy through direct payments is considered gross income and cannot be used to offset the mortgage payment directly, even if the employer pays the servicing creditor directly.
   - **Retirement income or Social Security income** – The income may not be considered effective if it will expire within the first three years after closing.
   - **Automobile allowances and expense account payments** – A creditor must consider only the amount by which the consumer's automobile allowance or expense-account payments exceed actual expenditures.
4. **Consumers employed by a family-owned business.** In addition to normal employment verification, a consumer employed by a family-owned business must provide evidence that he/she is not an owner of the business.
5. **Self-employed consumers.** A consumer with a 25% or greater ownership interest in a business is considered self-employed. Income from self-employment generally may be considered effective only if the consumer has been self-employed for two or more years. For consumers who have been self-employed for between one and two years, additional employment and educational information is required. Income from consumers who have less than one year of self-employment cannot be considered effective. When qualifying a self-

[5] As an example, for consumers planning to retire during the first three-year period, the effective income must include documented retirement benefits, Social Security, and other expected payments.

employed consumer for a mortgage loan, the creditor must establish the consumer's earnings trend from the previous two years and analyze the business's financial strength. The CFPB has proposed to eliminate, rather than clarify, some aspects of the requirement to analyze the business's financial strength.

6. **Guidance on income analysis.** A creditor must collect sufficient information and analyze tax returns in order to determine a consumer's compensation. The appendix sets forth specific guidance regarding the use of tax returns to conduct an income analysis for individuals, corporations, S-corporations, and partnerships.

II. Non-employment-related consumer income

A. General requirements.

A creditor must properly verify, analyze, and document non-employment-related consumer income for qualifying purposes. The rule contains specific requirements on the length of time in which the income payment has been consistent and/or will continue. For certain forms of income, additional requirements may apply.

B. Alimony, child support, and maintenance income.

Alimony, child support, and maintenance income generally may be considered effective if it has been received during the past 12 months and payments will continue for the first three years of mortgage.

C. Investment and trust income.

Specific criteria apply to investment and trust income. Interest and dividends must be supported by a two-year receipt history and averaged over two years, less any such funds used for the down payment. For trust income, a creditor must verify that guaranteed, consistent payments will continue for the first three years of the mortgage loan. For notes-receivable income, a creditor must verify these payments have been consistently received for the last 12 months. Income from eligible investment properties may be considered, unless the monthly payment (PITI) exceeds the monthly net rental income. The CFPB has proposed technical revisions to the trust income and notes-receivable income provisions.

D. Military, government-agency, and assistance-program income.

Military income may be considered in calculating the debt-to-income ratio, including such forms of pay as variable housing allowances, clothing allowances, flight or hazard pay, rations, and proficiency pay, as long as the probability of such pay to continue is verified in writing. VA benefits may be considered in calculating the debt-to-income ratio if the creditor receives documentation from the VA, but VA education benefits used to offset education expenses are not acceptable.

Income from government assistance programs may be considered if expected to continue for at least three years and supported by documentation from the paying agency. Unemployment income may be considered if documented for two years and continuity is reasonably assured. Mortgage payments subsidized by a government entity through direct payments or tax rebates may be considered, and may be added to gross income, or used directly to offset the mortgage payment. A monthly subsidy under the housing-choice voucher homeownership option from a public housing agency may be treated as income and is assumed to continue for at least three years.

E. Rental income.

Rental income from properties owned by the consumer may be included, as long as the creditor can document the stability of the income through a current lease, an agreement to lease, or a rental history over the previous 24 months that is free of unexplained gaps greater than three months. Rent from tenant-occupied units in a consumer-owned and -occupied multiple-unit property may be used for qualifying purposes, but income from roommates in a single-family property occupied as the consumer's primary residence generally cannot be considered. Special rules apply to exclude from consideration rental income from a principal residence that is being vacated in favor of another principal residence.

1. **Required documentation.** The documentation required to verify rental income includes: (1) IRS Form 1040 Schedule E and (2) current leases/rental agreements.
2. **Rental income calculation.** A creditor must: (1) reduce the gross rental amount by 25% for vacancies and maintenance; (2) subtract PITI and any homeowners' association dues; and (3) apply the resulting amount to income, if positive, or recurring debts, if negative.

F. Non-taxable and projected income.

1. **Non-taxable income.** The amount of continuing tax savings attributed to regular non-taxable income, such as railroad retirement benefits and some government retirement income, may be added to the consumer's gross income. The creditor must document and support the amount of income grossed up for any non-taxable income source and should use the tax rate used to calculate the consumer's last year's income tax, or use 25% if no Federal tax return was required to be filed.
2. **Projected income.** Projected income cannot be considered, except (a) for income from cost-of-living adjustments, performance raises, and bonuses verified in writing by the employer and scheduled to begin within 60 days of loan closing, or (b) if a consumer is scheduled to start a new job within 60 days of loan closing under a guaranteed, non-revocable employment contract.

III. Consumer liabilities: Recurring obligations

Recurring obligations include all installment loans, revolving charge accounts, real estate loans, alimony, child support, and other continuing obligations. When computing the debt-to-income ratios for recurring obligations, a creditor must include the monthly housing expense and additional recurring charges extending ten months or more into the future. Debt lasting less than ten months must be included if it affects the consumer's ability to pay the mortgage during the months immediately after loan closing. Monthly payments on revolving or open-ended accounts are counted as a liability for qualifying purposes even if the account appears likely to be paid off within 10 months or less. If the credit report shows any revolving accounts with no specific minimum monthly payment, the payment must be calculated as the greater of 5% of the balance or $10. If the actual monthly payment is documented, that amount may be used.

IV. Consumer liabilities: Contingent liability

A contingent liability must be considered unless the consumer can provide conclusive evidence from the debt holder that there is no possibility that the debt holder will pursue debt collection against him/her should the other party default. Specific standards apply to contingent liabilities relating to the sale or assumption of a mortgage without a release of liability or the applicant acting as co-signer or co-obligor on another obligation.

V. Projected obligations and obligations not considered debt

A. Projected Obligations.

Debt payments anticipated in the coming 12 months, including balloon-payment notes, must be included in the underwriting analysis, unless the consumer provides written evidence that the debt payments have been deferred to a period outside the 12-month timeframe.

B. Obligations Not Considered Debt.

Obligations not considered debt, and therefore not subtracted from gross income, include: (1) federal, state, and local taxes; (2) Federal Insurance Contributions Act (FICA) or other retirement contributions; (3) commuting costs; (4) union dues; (5) open accounts with zero balances; (6) automatic deductions to savings accounts; (7) child care; and (8) voluntary deductions.

Mortgage-Servicing Final Rules

Effective date: January 10, 2014

I. Overview

The final rules set forth requirements addressing each of the following: (1) periodic billing statements; (2) initial rate adjustment notices; (3) prompt crediting of mortgage payments, and responses to requests for payoff amounts; (4) error resolution and information requests; (5) force-placed insurance requirements; (6) general servicing policies and procedures to achieve certain objectives set forth in the rules; (7) early intervention with delinquent borrowers; (8) continuity of contact with delinquent borrowers; and (9) loss-mitigation procedures, including limitations on dual tracking. The first three issues are addressed in Regulation Z (Truth in Lending Act) and the remaining six issues are addressed in Regulation X (Real Estate Settlement Procedures Act). Each aspect of the mortgage-servicing rules is discussed in detail below.

II. Periodic billing statements

A creditor, assignee, or servicer of a closed-end consumer credit transaction secured by a dwelling generally must provide a periodic statement for each billing cycle containing certain information specified in the rule. Certain exemptions apply to reverse mortgages, timeshare plans, coupon books for fixed-rate mortgages, and small servicers. These statements must meet the timing, form, and content requirements provided in the rule, as described below. The rule contains model and sample forms to facilitate compliance. These provisions are subject to both administrative enforcement and private rights of action.

A. Scope.

The rule applies to closed-end mortgage loans secured by a dwelling, except when such loans satisfy the reverse mortgage, timeshare plan, coupon book, or small-servicer exemptions described in detail below.

B. Timing.

The periodic statement must be delivered or placed in the mail within a reasonably prompt time after the payment due date or the end of any courtesy period provided for the previous billing cycle. Generally, four days after the end of the courtesy period of the previous billing cycle is considered reasonably prompt.

C. Form.

The periodic statement must be clear and conspicuous, in writing, or electronically if the consumer agrees, and provided in a form that consumers may keep. Proper use of the model forms satisfies these requirements.

D. Content.

The following items must be included in the statements:

1. **Amount due.** The information must include: (1) amount due, (2) payment due date, and (3) the amount of any late-payment fee and the date on which it will be imposed.
2. **Explanation of amount due.** The creditor must explain: (1) the monthly payment amount, including a breakdown of how the payment will be applied to principal, interest, and escrow; (2) total sum of any fees or charges imposed since the last statement; and (3) any payment amount past due.
3. **Past-payment breakdown**. Payment breakdown includes: (1) the total of all payments received since the last statement, including a breakdown of how those funds were applied to principal, interest, escrow, fees and charges, and, if applicable, a suspense or unapplied-funds account; (2) the total of all payments received since the beginning of the current calendar year, including a breakdown of how those funds were applied to the categories described above.
4. **Transaction activity.** A list of transaction activities, including the date, a brief description, and amount of the transaction.
5. **Partial-payment information**. If the statement reflects a partial payment placed in a suspense or unapplied-funds account, information explaining what must be done in order for the funds in the suspense or unapplied account to be applied.
6. **Contact information.** A toll-free telephone number and, if applicable, an email address for the consumer to obtain account information.
7. **Account information.** The creditor must provide: (1) the amount of the outstanding principal balance, (2) the current interest rate, (3) the date of the next possible interest-rate change, (4) the existence of a prepayment penalty, and (5) a website to access either the CFPB- or HUD-approved lists of homeownership counselors and counseling organizations.
8. **Delinquency information.** If the consumer is more than 45 days delinquent, the following items must be grouped together in close proximity on the first page of the statement: (1) the date of delinquency; (2) a notification of possible risks to the consumer, including foreclosure and expenses; (3) account history for the shorter of the last six months or the last time the account was current; (4) a notice of any loss-mitigation program to which the consumer has agreed; (5) a notice of whether the servicer has made its first legal filing or notice required to commence the foreclosure process; (6) the total payment needed to bring the account current; and (7) a reference to homeownership counseling information.

C. Exemptions.

The rule provides the four exemptions to the periodic-statement requirement for:

1. Reverse mortgages;
2. Transactions secured by timeshare plans;
3. Fixed-rate mortgages where the servicer provides consumers coupon books containing certain information specified in the rule and certain other information specified in the rule is made available to the consumer; and

4. The servicer is a small servicer that services 5,000 or fewer mortgage loans if, for all of those loans, the servicer (or an affiliate) is the creditor or assignee, or if servicing is provided by a Housing Finance Agency. On May 2, 2013, the CFPB proposed to clarify the small-servicer exemption by stating that certain types of loans — reverse mortgages, mortgages secured by timeshare plans, and certain mortgages serviced voluntarily without remuneration — are not considered in making the small-servicer determination.

III. Interest-rate adjustment notices for ARMs

Creditors, assignees, and servicers must provide a consumer with an adjustable-rate mortgage (ARM) secured by the consumer's principal dwelling with a notice between 210 and 240 days prior to the first payment due after the initial interest-rate adjustment. This one-time notice may contain an estimate of the new rate and new payment.

For the same loans described above, creditors, assignees, and servicers also must provide a notice between 60 and 120 days before payment at a new level is due when any rate adjustment causes the payment to change. Special timing rules apply to ARMs with uniformly scheduled interest-rate adjustments occurring every 60 days or less and to certain ARMs originated prior to January 10, 2015, with specific contract requirements. The current annual notice that must be provided for ARMs for which the interest rate, but not the payment, has changed will be eliminated. The rule contains model and sample forms that servicers may use. These provisions are subject to both administrative enforcement and private rights of action.

A. Scope.

The rule applies to closed-end adjustable-rate mortgage loans secured by a consumer's principal dwelling, including the conversion of an adjustable-rate mortgage to a fixed-rate transaction.

B. Timing.

Timing requirements are specified in the summary above.

C. Form.

The disclosures must be clear and conspicuous, in writing, or electronically if the consumer consents, and in a form the consumer may keep.

D. Content.

The content of the one-time, initial interest-rate adjustment notice and the notice required in connection any payment change caused by an interest-rate adjustment are substantially similar, except as noted in D.8. below and the fact that estimates may be provided in the one-time notice. The content includes the following items:

1. A statement providing an explanation that under the terms of the consumer's ARM, the time period in which the current interest rate has been in effect is ending and the interest rate and mortgage payment will change; the effective date of the interest-rate adjustment and when future interest-rate adjustments are scheduled to occur; and any other changes to loan terms, features, or options taking effect on the same date as the interest-rate adjustment.

2. A table containing: the current and new interest rates and payments; the due date for the first new payment; and for interest-only or negatively-amortizing payments, the current and new payment allocations to principal, interest, and escrowed taxes and insurance.
3. An explanation of how the interest rate is determined, including the index or formula used and the type and amount of any adjustment to the index.
4. Any limits on interest-rate or payment increases at each adjustment and over the life of the loan, including the earliest date on which any foregone interest-rate increases may apply.
5. An explanation of how the new payment is determined, including the index or formula used, any adjustments to such index or formula, the loan balance expected on the date of the adjustment, and the expected length of the remaining loan term on the date of the adjustment.
6. If applicable, a statement that the new payment will not be allocated to pay loan principal and will not reduce the loan balance.
7. The circumstances under which a payment penalty may be imposed, the time period when a penalty may be imposed, and statement that the consumer may request for additional information, including maximum amount of penalty.
8. The initial rate-adjustment notices must also include the date of disclosure, a statement that further notice will be provided if the new interest rate and payment are an estimate, the telephone number for consumers to call in case of delinquency or expected delinquency, a list and brief explanation of alternatives to delinquency, such as refinancing and loan modification, and homeownership counseling information.

E. Exemption.

The initial adjustment notice does not apply to ARMs with a term of one year or less or if the initial rate adjustment is within 210 days after consummation and the new interest rate is disclosed at consummation. Also, ARMS do not include shared equity or shared-appreciation mortgages.

IV. Prompt payment crediting and payoff statements

The final rules amend certain existing requirements relating to prompt crediting and payoff statements. These provisions are subject to both administrative enforcement and private rights of action.

A. Prompt crediting.

A servicer must promptly credit periodic payments (principal, interest, and escrow) from a borrower as of the day of receipt, except when:

1. A delay in crediting does not result in any charge to the consumer, nor does it result in the reporting of negative information to a consumer reporting agency;
2. If the payment does not conform to the requirements specified by the servicer in writing for making payments, but the servicer accepts the payment, the servicer must credit the payment as of five days after receipt.

B. Partial payments.

If a servicer receives a payment that is less than the amount due for a periodic payment, the payment may be held in a suspense or unapplied-funds account. When the amount in the suspense account accumulates to an amount equal to a periodic payment, the servicer must apply the funds to the consumer's account.

C. No pyramiding of late fees.

A servicer may not impose any late fee or delinquency charge on a payment if (a) the payment is a periodic payment received by the due date or applicable courtesy period, and (b) the fee or charge is attributable solely to the failure of a consumer to pay a late fee or delinquency charge on an earlier payment.

D. Payoff balances.

Creditors, assignees, and servicers must provide an accurate payoff balance to a consumer no later than seven business days after receipt of a written request from the borrower for such information.

V. Force-placed insurance

The final rules impose limitations on servicers' obtaining force-placed insurance. These provisions are subject to both administrative enforcement and private rights of action.

A. Reasonable basis.

A servicer is prohibited from charging a borrower for force-placed insurance coverage unless the servicer has a reasonable basis to believe the borrower has failed to maintain hazard insurance and has provided the required notices to the consumer.

B. Escrow.

Where the borrower has an escrow account for the payment of hazard insurance premiums, the servicer is prohibited from obtaining force-place insurance if the servicer can continue the borrower's homeowner insurance, even if the servicer needs to advance funds to the borrower's escrow account to do so. A servicer is considered unable to disburse funds through an escrow account only if the servicer reasonably believes that the borrower's hazard insurance policy was canceled for reasons other than nonpayment of premium charges or that the property is vacant. However, a servicer that services 5,000 or fewer mortgage loans – if, for all those loans, the servicer (or an affiliate) is the creditor or assignee, or a servicer that is a housing finance agency — is exempt from the requirement to disburse or advance funds from an escrow account, provided that any force-placed insurance purchased by the servicer is less expensive to a borrower than the amount of any disbursement the servicer would have made from the escrow account to maintain hazard insurance coverage.

C. Scope.

The following types of insurance are <u>not</u> considered force-placed: (a) hazard insurance required by the Flood Disaster Protection Act of 1973; (b) hazard insurance obtained by a borrower but renewed by the servicer through the disbursement or advancing of funds from the borrower's escrow account; and (c) hazard insurance obtained by a borrower but renewed by the borrower's servicer at its discretion, if the borrower agrees.

D. Notices.

To establish a reasonable basis for obtaining force-placed insurance, a servicer must provide to the borrower two notices prior to charging the borrower for force-placed insurance. An initial notice must be sent to the borrower at least 45 days before charging the borrower for force-placed insurance. A second reminder notice must be sent to the borrower no earlier than 30 days after the first notice and at least 15 days before charging the borrower for force-placed insurance. The content requirements of the two notices are specified in the rule and model forms to facilitate compliance and are provided in an appendix to the rule.

E. Renewal or replacement notices.

A servicer must provide the borrower with a written notice of renewing or replacing an existing force-placed insurance at least 45 days before assessing a charge or fee for the renewal or replacement. A servicer must also have no evidence demonstrating that the borrower has purchased the hazard insurance coverage required by the loan contract. The content of the renewal or replacement notice is specified in the rule and model forms to facilitate compliance are provided in an appendix to the rule.

F. Cancellation and refund.

If a borrower provides proof of hazard insurance coverage, the servicer must cancel any force-placed insurance policy and refund any premiums paid for overlapping periods during which the borrower's coverage was in place.

G. Reasonableness of charges.

Charges related to force-placed insurance (other than those subject to state regulation as the business of insurance or authorized by federal law for flood insurance) must be for a service that was actually performed and must bear a reasonable relationship to the servicer's cost of providing the service.

VI. Error resolution and information requests

A servicer is required to meet certain procedural requirements for responding to written notices from a borrower or a borrower's representative asserting an error or requesting information. A written notice from a borrower must include the name of the borrower and enable the servicer to identify both the borrower's mortgage loan account and the alleged error.

A. Error Resolution

1. **Errors.** Under the rule, "errors" include the following:
    - **a.** Failure to accept a payment that conforms to the servicer's written requirements;
    - **b.** Failure to apply an accepted payment in compliance with the loan terms and applicable laws;
    - **c.** Failure to credit a payment to a borrower's mortgage loan account as of the date of receipt;
    - **d.** Failure to pay taxes, insurance premiums, or other charges in a timely manner, or to refund an escrow account balance as required;

   e. Imposition of a fee or charge that the servicer lacks a reasonable basis to impose;
   f. Failure to provide information to a borrower regarding loss-mitigation options and foreclosure;
   g. Failure to transfer accurately and timely information relating to the servicing of a borrower's mortgage loan account to a transferee servicer;
   h. Making the first notice or filing to begin a foreclosure process in violation of other requirements of the final rule;
   i. Moving for foreclosure judgment or order of sale, or conducting a foreclosure sale in violation of other requirements of the final rule; and
   j. Any other error relating to the servicing of a borrower's mortgage loan.

2. **Error-resolution procedures.** The following procedures must be followed by servicers in connection with receipt of a notice of error.
   a. **Designate address for notices of error and information requests.** A servicer may designate a specific address for borrowers to submit both written error notices and information requests. To do so, a servicer must provide a written notice to the borrower regarding the designated address, post the designated address on any website maintained by the servicer that lists any contact address for the servicer, and provide the designated address to the borrower in any communication in which the servicer provides the borrower with contact information for assistance. Designating a specific address is not required; however, if a servicer does not designate an address, it must respond to any notice of error or information request received by any office of the servicer.
   b. **Acknowledgement.** A servicer generally must acknowledge receipt of a notice of error in writing within five business days, unless:
      - The servicer corrects the error and notifies the borrower in writing of the correction within five business days; or
      - The servicer receives the notice of error seven or fewer days before a foreclosure sale.
   c. **Response.** Except in cases where no acknowledgement is required, a servicer generally must respond to the notice of error within the timeframes outlined below by:
      - **Error** – Correcting the error asserted by the borrower and providing the borrower written notification of the correction and its effective date, along with contact information for further information;
      - **No error** – Conducting an investigation and providing the borrower written notification that no error occurred, the reasons for this determination, the borrower's right to request documents relied upon in reaching this determination and how to request them, and contact information for further assistance. A servicer must provide, at no cost, copies of documents relied upon in its determination that no error occurred within 15 business days of receiving a

borrower's request for such documents,[6] although confidential, privileged, or proprietary documents may be withheld if the borrower is notified; or

- **Different or additional error** – If a different or additional error is found to have occurred, correcting the error and providing the borrower written notification of the error identified, action taken to correct the error and its effective date, and contact information for further assistance.

d. **Exceptions.** A servicer is not required to comply with the error-resolution procedures if the servicer reasonably determines that:

- **Duplicative notice** – The asserted error is substantially the same as a previously asserted error, unless the borrower provides new and material evidence to support the claim of error;
- **Overbroad notice** – The notice is overbroad, such that the servicer cannot reasonably determine from the notice the specific error the borrower is asserting; or
- **Untimely notice** – The notice is delivered to the servicer more than one year after servicing for the mortgage has been transferred to a transferee servicer or the mortgage loan balance has been paid in full.

e. **Borrower cooperation.** A servicer may request information from a borrower to support the assertion of an error, but may not make receipt of such information from the borrower a condition of investigating an alleged error or determine that no error occurred because a borrower did not provide the requested information.

3. **Timing.** The servicer must investigate the alleged error and respond to the consumer generally within 30 days after receipt of the notice of error, excluding weekends and legal public holidays. The servicer may extend the response deadline to 45 days by providing written notice of the extension to the borrower and the reasons for the extension before the end of the 30-day period, except for errors subject to the special timing deadlines described below.

   Special timing deadlines apply in the following circumstances:

   a. No later than seven business days after receipt of the notice of error if the error is the failure to provide payoff balance statement; and

   b. Prior to the date of a foreclosure sale or within 30 business days after the receipt of the error notice, whichever is earlier, for errors related to a foreclosure process.

4. **Fees.** A servicer is prohibited from charging fees, or requiring a borrower to make any payment that may be owed, as a condition for responding to a notice of error.

B. Information Requests

1. **Acknowledgement.** A servicer is generally required to acknowledge in writing a borrower's written request for information within five business days of receipt.

[6] The rule is not clear as to whether a borrower request for copies of documents can be made orally as well as in writing.

2. **Response.** A servicer must respond to an information request by either providing the information requested or explaining in writing why, after conducting a reasonable search, the information is not available.
3. **Timing.** A servicer must respond to a borrower's information request:
   a. No later than 10 business days after receipt of a request for the identification of, and address or other relevant contact information for, the owner or assignee of a mortgage loan; and
   b. No later than 30 business days for all other information requests, although this can be extended to 45 business days if the servicer notifies the borrower in writing of the extension and the reasons for the extension before the end of the 30-day period.
4. **Exceptions.** Subject to providing written notice to the borrower within five business days of making one of the determinations below, the requirements to respond to information requests do not apply to requests for:
   a. Duplicative information that is substantially the same as information previously requested and provided;
   b. Confidential, proprietary, or privileged information;
   c. Irrelevant information;
   d. Overbroad or unduly burdensome requests that seek an unreasonable volume of documents or information or that a diligent servicer could not respond to within the maximum time limit or without incurring unreasonable costs; and
   e. Requests made more than one year after the transfer of servicing for the mortgage loan to a transferee servicer or payment in full of the mortgage loan balance.
5. **Fees.** A servicer generally is prohibited from charging fees, or requiring a borrower to make any payment that may be owed, as a condition for providing requested information.

VII. General servicing policies, procedures, and requirements

A servicer is required to maintain policies and procedures reasonably designed to achieve certain objectives specified in the rule. The reasonableness of a servicer's policies and procedures takes into account the size, scope, and nature of the servicer's operations.

A. Objectives.

A servicer's policies and procedures must be reasonably designed to ensure that the servicer can:

1. **Access and provide timely and accurate information to the borrower and other relevant parties.** This includes: (1) providing accurate and timely disclosures to a borrower; (2) investigating, responding to, and correcting errors asserted by the borrower; (3) providing accurate and timely information to borrowers in response to information requests; (4) providing accurate and current information to owners or assignees about the mortgage loans they own; (5) submitting foreclosure-related documents or filings that reflect accurate

and current information and that comply with applicable law; and (6) promptly identifying and facilitating communication with the successor in interest of a deceased borrower upon notification of the death of a borrower.

2. **Properly evaluate loss-mitigation applications.** This includes: (1) providing accurate information to a borrower about available loss-mitigation options; (2) identifying with specificity all loss-mitigation options for which a borrower may be eligible; (3) providing all servicer personnel assigned to assist the borrower under the continuity-of-contact provision, discussed below, with prompt access to all documents and information submitted by a borrower in connection with a loss-mitigation option; (4) identifying documents and information that a borrower must submit to complete a loss-mitigation application in order to notify the borrower of the same; and (5) properly evaluating a borrower who submits a complete application for a loss-mitigation option for all options for which the borrower may be eligible.
3. **Facilitate oversight of, and compliance by, service providers.** This includes: (1) providing appropriate servicer personnel with accurate and current documents and information regarding actions performed by service providers; (2) facilitating periodic reviews of service providers for compliance with contractual obligations and applicable law; and (3) facilitating the sharing of accurate and current information regarding the status of a borrower's loss-mitigation application and the status of a foreclosure proceeding among appropriate servicer and service-provider personnel.
4. **Facilitate the transfer of information during servicing transfers.** This includes: (1) timely transferring of all information and documents relating to a borrower's mortgage loan to a transferee servicer in a form and manner that ensures accuracy and enables the transferee servicer to comply with its obligations; and (2) for the transferee servicer, identifying and obtaining from the transferor servicer any necessary documents or information that may not have been transferred.
5. **Inform borrowers of the procedures for submitting written notices of error and written information requests.**

B. Record-retention requirements.

A servicer must retain records that document actions taken with respect to a borrower's mortgage loan until one year after the discharge of the loan or the transfer of servicing rights. In addition, a servicer must also maintain the following documents in a manner that facilitates compiling them into a servicing file within five days: a schedule of all transactions credited or debited to the mortgage loan account; a copy of the security instrument that established the lien securing the mortgage loan; any notes created by servicer personnel reflecting communications with the borrower about the mortgage loan account; a report of the data fields relating to the borrower's mortgage loan created by the servicer's electronic systems in connection with servicing practices, if applicable; and copies of any information or documents provided by the borrower in connection with a written notice of error or a loss-mitigation application.

C. Small-servicer exemption.

There is an exemption from these requirements for a servicer that services 5,000 or fewer mortgage loans if, for all of those loans, the servicer (or an affiliate) is the creditor or assignee, and for a servicer that is a Housing Finance Agency.

D. No private right of action.

The bureau and the prudential regulators will be able to supervise servicers within their jurisdiction to assure compliance with these requirements. However, these provisions may not be enforced through private rights of action.

VIII. Early intervention with delinquent borrowers

The final rule requires servicers to engage in early intervention with delinquent borrowers. These provisions are subject to both administrative enforcement and private rights of action.

A. Oral contact.

A servicer must establish or make good-faith efforts to establish live contact with a delinquent borrower no later than the 36th day of the delinquency and promptly inform such borrowers that loss mitigation options may be available, if appropriate.

B. Written notice.

In addition, a servicer must provide a borrower a written notice with information about loss-mitigation options no later than the 45th day of the borrower's delinquency. This notice is only required to be provided once during any 180-day period. The written notice must contain the following information: a statement encouraging the borrower to contact the servicer; the servicer's telephone number for contacting or reaching personnel responsible for continuity of contact and the servicer's mailing address; a brief description of examples of loss-mitigation options available from the servicer, if applicable; a statement regarding how to obtain more information regarding loss-mitigation options from the servicer, if applicable; and the bureau or HUD website listing homeownership counselors and organizations. Model clauses for the written notice are provided in an appendix.

C. Small-servicer exemption.

The early-intervention requirement does not apply to a servicer that services 5,000 or fewer mortgage loans if, for all those loans, the servicer (or an affiliate) is the creditor or assignee, or a servicer that is a housing finance agency.

IX. Continuity of contact with delinquent borrowers

A. General requirements.

A servicer is required to maintain reasonable policies and procedures to achieve the following three objectives:

1. Assign personnel to a delinquent borrower by the time the servicer provides the written early-intervention notice, but in any event, not later than the 45th day of the borrower's delinquency;
2. Make available to a delinquent borrower, via telephone, personnel assigned to respond to borrower inquiries and assist the borrower with available loss-mitigation options; and

3. Ensure that the servicer can provide a live response from assigned personnel in a timely manner if the borrower contacts the servicer but does not immediately receive a live response.

The servicer personnel assigned to assist a delinquent borrower must remain accessible to the borrower until the borrower has made two consecutive mortgage payments in accordance with a permanent loss-mitigation agreement without incurring a late charge.

The servicer must maintain policies and procedures reasonably designed to ensure that the assigned personnel can perform the following functions:

1. Provide the borrower with accurate information about loss-mitigation options available to the borrower; actions the borrower must take to be evaluated for such options, including completing a loss-mitigation application or appealing a denial of an application; the status of any loss-mitigation application submitted by the borrower; the circumstances under which the servicer may refer to foreclosure; and loss-mitigation timelines.
2. Retrieve in a timely manner a complete record of the borrower's payment history and all written information the borrower has provided to the servicer or prior servicers in connection with a loss-mitigation application, and provide that information, when appropriate, to those responsible for evaluating the borrower for loss-mitigation options.
3. Provide a delinquent borrower with information about how to submit a written notice of error or information request.

B. Small-servicer exemption.

The continuity-of-contact requirements do not apply to a servicer that services 5,000 or fewer mortgage loans if, for all those loans, the servicer (or an affiliate) is the creditor or assignee, or a servicer that is a housing finance agency.

C. No private right of action.

The bureau and the prudential regulators will be able to supervise servicers within their jurisdiction to assure compliance with these requirements. However, these provisions may not be enforced through private rights of action.

X. Loss-Mitigation Procedures

The final rule prohibits foreclosure referrals and foreclosures sales in certain circumstances and requires servicers to follow specified loss-mitigation procedures in connection with considering a borrower's loss-mitigation application. These provisions are subject to both administrative enforcement and private rights of action.

A. Dual-tracking restrictions.

The rule imposes certain restrictions on "dual tracking". Dual tracking occurs when a servicer is simultaneously evaluating a borrower for loan modifications or other loss-mitigation alternatives at the same time that it is pursuing foreclosure on the property.

1. **Prohibition on foreclosure referral.** A servicer is prohibited from making the first notice or filing required by applicable law to begin the foreclosure process until a mortgage loan

account is more than 120 days delinquent. In addition, if a borrower submits a complete application for a loss-mitigation option before a servicer has made the first notice or filing required by applicable law to begin the foreclosure process, even if a borrower is more than 120 days delinquent, a servicer is prohibited from initiating the foreclosure process, unless (1) the servicer notifies the borrower in writing that the borrower is not eligible for any loss-mitigation option (and any appeal right has been exhausted), (2) a borrower rejects all loss-mitigation offers, or (3) a borrower fails to perform under the terms of a loss-mitigation option, including a trial modification.

2. **Prohibition on foreclosure sale.** If a borrower submits a complete application for a loss-mitigation option after the servicer has initiated the foreclosure process by making the first notice or filing required by applicable law, but more than 37 days before a foreclosure sale, a servicer is prohibited from moving for a foreclosure judgment or order of sale, or conducting a foreclosure sale, until one of the same three conditions described in the previous paragraph has been satisfied. The servicer is responsible for promptly instructing foreclosure counsel retained by the servicer not to proceed with filing for foreclosure judgment or order of sale, or to conduct a foreclosure sale, as applicable, and to take reasonable steps to avoid a ruling on a previously filed dispositive motion.

B. Procedures for handling and evaluation loss-mitigation applications

1. **Receipt of a loss-mitigation application.** If a borrower submits an application for a loss-mitigation option 45 days or more before a foreclosure sale, a servicer must promptly review the application for completeness, acknowledge the receipt of the application in writing within five business days, and inform the borrower whether the application is complete and, if not, identify the additional documents or information necessary to complete the application. The notice must state the deadline for receiving additional documents, which is the earliest remaining date of: the date by which any document submitted will be considered stale or invalid, the 120th day of the borrower’s delinquency, the 90th day before a foreclosure sale, or the 38th day before a foreclosure sale. The servicer must exercise reasonable diligence in obtaining documents and information to complete the application. The official interpretations provide an expansive interpretation of what constitutes a “loss-mitigation application.” If a borrower expresses an interest in applying for a loss-mitigation option and provides any information that the servicer would evaluate in connection with such an application, then the communication is treated as a loss-mitigation application.

2. **Evaluation of a loss mitigation application.**

   a. **Complete application.** For a complete loss-mitigation application received more than 37 days before a foreclosure sale, the servicer must evaluate the borrower, within 30 days, for all loss-mitigation options for which the borrower may be eligible in accordance with the investor’s eligibility rules and notify the borrower in writing of which options, if any, the servicer will offer to the borrower. The evaluation must include both options that enable the borrower to retain the home (such as a loan modification) and non-retention options (such as a short sale). Servicers are free to follow an order ranking for evaluation of loan-modification options, commonly known as a “waterfall,” established by an investor to determine eligibility for particular loss-mitigation options.

b. **Incomplete application.** A servicer is prohibited from evading the requirement to evaluate a complete loss-mitigation application for all available loss-mitigation options by offering an option based on an evaluation of an incomplete application. However, if the servicer has exercised reasonable diligence but the application remains incomplete for a significant period of time (which depends on the circumstances, including the timing of the foreclosure process), the servicer may evaluate an incomplete loss-mitigation application and offer a borrower a loss-mitigation option.

3. **Notice of denial.** If a borrower's complete loss-mitigation application is denied for one or more available trial or permanent modification options, the servicer must include in the written notice the specific reasons for denying the borrower for each such option and a statement about the borrower's right to appeal and the timeframe and requirements for making an appeal. This requirement applies even if the borrower is approved for one or more other trial or permanent modification options. Where the denial is based on investor requirements, the specific reasons must identify the investor and the requirement that is the basis of the denial. Where the denial is based on a net-present-value calculation, the specific reasons must include any inputs used to make the net-present-value calculation to the extent such inputs were the basis for the denial.

4. **Borrower response.**

   a. If a complete loss-mitigation application is received by a servicer 90 days or more before a foreclosure sale, the servicer may require that a borrower accept or reject an offer of a loss-mitigation option no earlier than 14 days after the servicer provides the offer to the borrower.

   b. If the application is received by a servicer more than 37 but less than 90 days before a foreclosure sale, the servicer may require that a borrower accept or reject an offer of a loss-mitigation option no earlier than 7 days after the servicer provides the offer to the borrower.

   c. A servicer may deem a borrower to have rejected an offer if the borrower does not accept an offer within the timeframes outlined above. However, if a borrower submits the payments required under a trial modification plan, but does not meet all the requirements for accepting the offer, the borrower must be given an additional reasonable period of time to accept the trial modification plan beyond the deadlines discussed above. If a borrower appeals the denial of any available trial or permanent loan-modification program, the deadline for accepting a loss-mitigation option is extended until 14 days after the servicer provides the written notice of appeal determination.

5. **Borrower appeal.** A borrower may appeal a denial of a loss-mitigation application for any trial or permanent loan-modification program available to the borrower, so long as the borrower's complete loss-mitigation application is received during the first 120 days of the borrower's delinquency or 90 days or more before a scheduled foreclosure sale. A servicer shall permit a borrower to make an appeal within 14 days after the servicer provides the offer of a loss-mitigation option. The appeal must be reviewed by different personnel from those responsible for evaluating the borrower's complete loss-mitigation application. The servicer must provide a notice to the borrower within 30 days of a borrower making an

appeal stating the servicer's determination of whether it will offer the borrower a loss-mitigation option based on the appeal. As noted above, a servicer may require that a borrower accept or reject an offer of a loss-mitigation option after an appeal, no earlier than 14 days after the servicer provides the notice. The decision is not subject to any further appeal.

C. Small-servicer exemption.

For a servicer that services 5,000 or fewer mortgage loans — if, for all those loans, the servicer (or an affiliate) is the creditor or assignee, or a servicer that is a housing finance agency — only two of the requirements of the loss-mitigation rules apply. First, a small servicer is prohibited from making the first notice or filing required to begin the foreclosure process, unless a borrower is more than 120 days delinquent. Second, if a borrower is performing pursuant to the terms of a loss-mitigation agreement, a small servicer may not make the first notice or filing required to begin the foreclosure process, move for foreclosure judgment or order of sale, or conduct a foreclosure sale.

High-Cost Mortgage and Homeownership-Counseling Amendments

Effective Date: January 10, 2014

I. Overview

The final rule expands the tests for coverage under the Home Ownership and Equity Protection Act of 1994 (HOEPA) to capture a broader segment of mortgage loans as "high-cost mortgages." The rule also adds protections for consumers in connection with high-cost mortgages, including a requirement that borrowers receive homeownership counseling before obtaining a high-cost mortgage.

High-cost mortgages are subject to special disclosure requirements and restrictions on certain loan terms. In addition, consumers who obtain high-cost mortgages have enhanced remedies for violations of law.

II. Scope

The final rule applies to all federally related mortgage loans, including most types of mortgage loans secured by a consumer's principal dwelling. The rule applies to purchase-money mortgages, refinanced mortgage loans, closed-end home-equity loans, and open-end credit plans (HELOCs).

III. Exemptions

The final rule does <u>not</u> apply to reverse mortgages, loans to finance the initial construction of a dwelling, loans originated by a Housing Finance Agency as the creditor, and loans originated through the US Department of Agriculture's Rural Housing Service Section 502 Direct Loan Program.

IV. Revised HOEPA coverage tests

A consumer credit transaction secured by the consumer's principal dwelling is deemed to be a **"high-cost mortgage"** if any one of the following tests is met:

A. Annual-percentage-rate (APR) test

1. APR Test

- **a.** The APR exceeds the applicable average prime offer rate by more than 6.5 percentage points for first-lien mortgage transactions with a loan amount equal to or greater than $50,000;
- **b.** The APR exceeds the applicable average prime offer rate by more than 8.5 percentage points for:

- First-lien mortgage transactions if the dwelling is personal property and the loan amount is of less than $50,000; and
- Subordinate-lien mortgages.

In contrast, the current triggers for high-cost mortgages are when the APR exceeds the yield on Treasury securities having comparable periods of maturity to loan maturity by 8.0 percentage points for first-lien mortgages and 10.0 percentage points for subordinate-lien mortgages.

2. **Determination of the APR.** The APR must be determined based on the following:
   a. For a non-variable APR, the interest rate in effect on the date the interest rate for the transaction is set;
   b. For a variable APR based on an index, the interest rate that results from adding the maximum margin permitted at any time during the loan or credit plan to the value of the index rate in effect on the date the interest rate for the transaction is set, or the introductory interest rate, whichever is greater;
   c. For a variable APR not based on an index, the maximum interest rate permitted under the loan or credit plan.
3. **Average prime offer rate.** The "average prime offer rate" means an APR that is derived from average interest rates, points, and other loan pricing terms currently offered to consumers by a representative sample of creditors for mortgage transactions that have low-risk pricing characteristics.

B. Points and fees test

1. The transaction's total points and fees exceed 5% of the total transaction amount for a transaction with a loan amount equal to or greater than $20,000; and
2. The transaction's total points and fees exceed 8% of the total transaction amount or $1,000, whichever is less, for a transaction with a total loan amount less than $20,000.[7]

For purposes of the HOEPA rules, the term "points and fees" has the same meaning as described in the Points and Fees Supplement to the Ability to Repay section above. For open-end credit transactions, "points and fees" include all of the fees or charges listed in the Points and Fees Supplement, along with the following two additions:

- **Participation fees.** Any fees charged for participation in an open-end credit plan payable at or before account opening; and
- **Transaction fees.** Any transaction fees charged for drawing on the credit line where the creditor must assume that the consumer will make at least one draw during the term of the plan.

[7] The $1,000 and $20,000 dollar amounts will be adjusted annually for inflation on January 1 by the annual percentage change in the consumer price index that was reported on the preceding June 1. The points and fees calculation is identical to the calculation of points and fees used for qualified mortgages.

C. Prepayment penalty test

The credit agreement permits the creditor to charge or collect a prepayment penalty:

1. More than 36 months after consummation or account opening; or
2. That can exceed, in total, more than 2% of the amount prepaid.

V. Prohibited acts or practices

The final rule implements the following new restrictions and requirements on loan terms and origination practices for high-cost mortgages.

A. A creditor is prohibited from originating an open-end, high-cost mortgage or HELOC without reasonably assessing the consumer's ability to repay.

B. A creditor or mortgage broker is prohibited from recommending or encouraging default on an existing loan prior to and in connection with the consummation or account opening of a high-cost mortgage.

C. No fee to modify, renew, extend or amend a high-cost mortgage, or to defer any payment due under the terms of such a mortgage, may be charged to the consumer.

D. Any late-payment fee imposed in connection with a high-cost mortgage must be specifically permitted by the loan terms, may not exceed 4% of the amount of the payment past due, and may be imposed only once for a single late payment.

1. A late-payment charge may be imposed in connection with a high-cost mortgage only if the payment is not received by 15 days after the due date, or, for a high-cost mortgage on which interest on each installment is paid in advance, 30 days after the due date.
2. The pyramiding of late fees is prohibited.
3. If the consumer fails to make a timely payment by the due date and subsequently resumes making payments but has not paid all past-due payments, the creditor may impose a separate late-payment charge for any payments outstanding.

E. A creditor is generally prohibited from charging a fee for providing to a consumer a statement of the amount due to pay off the outstanding balance of a high-cost mortgage. A creditor may charge a processing fee to cover the cost of providing a payoff statement by fax or courier if the fee is comparable to fees imposed in transactions that are not high-cost mortgages and a disclosure is provided to the consumer. Reasonable fees are also permitted if the borrower requests payoff statements more than four times during one calendar year. The payoff statement must be provided within five business days of receiving a request.

F. A creditor is prohibited from financing charges that are required to be included in the calculation of points and fees. Credit-insurance premiums or debt cancellation or suspension fees that are required to be included in points and fees are not considered financed by the creditor when they are calculated and paid in full on a monthly basis.[8]

[8] On May 29, 2013, the CFPB issued a final rule delaying the effective date of this provision until January 10, 2014, to allow for the clarification of the provision's applicability to transactions other than those in which a lump-sum premium is added to the loan amount at closing.

G. Balloon payments of more than two times a regular period payment are prohibited, unless the payment schedule is adjusted to the seasonal or irregular income of the consumer, the loan is a temporary bridge loan, or the loan is made by certain creditors operating predominantly in rural or underserved areas.

VI. Requirements for homeownership counseling for high-cost and other mortgages

A creditor is required to provide a clear, conspicuous, and recent written list of homeownership counseling organizations to a consumer within three business days after the consumer applies for a mortgage loan (excluding a reverse mortgage or a mortgage secured by a timeshare). A creditor must obtain the list from either a website that will be developed by the bureau, or data that will be made available by the bureau or HUD for compliance. A creditor does not have to provide the list if the application is denied or withdrawn within three business days.

A creditor is required to obtain a written certification from a federally certified homeownership counselor that the consumer has received counseling on the advisability of the mortgage before making a high-cost mortgage to a consumer. The counseling must occur after the consumer receives certain disclosures about the mortgage transaction. The counselor must not be employed by or affiliated with the creditor, but the creditor may pay the fees of a counselor or counseling organization. However, the creditor may not steer a consumer to a particular counselor or counseling organization.

A creditor must obtain confirmation that a first-time borrower has received homeownership counseling from a federally certified or approved homeownership counselor or counseling organization before making a loan that provides for or permits negative amortization.

Escrow Requirements

Effective date: June 1, 2013

I. Overview

Regulation Z currently requires creditors to establish escrow accounts for "higher-priced mortgage loans" to help ensure that consumers set aside funds to pay property taxes, premiums for homeowners insurance, and other mortgage-related insurance required by the creditor. The final rule lengthens the time for which a mandatory escrow account for a higher-priced mortgage must be maintained from one to five years. The final rule also exempts certain transactions from the escrow requirement.

II. Requirements

The final rule amends existing regulations that require creditors to establish and maintain escrow accounts for at least one year after originating a "higher-priced mortgage loan" to require generally that escrow accounts be maintained for such loans for at least five years.

For purposes of the rule, the term **"higher-priced mortgage loan"** means a closed-end consumer credit transaction secured by the consumer's principal dwelling with an APR that exceeds the average prime offer rate (APOR) by:

- 1.5 or more percentage points for first-lien conforming loans;[9]
- 2.5 or more percentage points for first-lien jumbo loans;[10] or
- 3.5 or more percentage points for subordinate-lien loans.

The **"average prime offer rate"** means an APR that is "derived from average interest rates, points, and other loan pricing terms currently offered to consumers by a representative sample of creditors for mortgage transactions that have low-risk pricing characteristics."

III. Exemptions

A. Current exemptions.

Regulation Z currently contains exemptions to the escrow requirement for transactions secured by shares in a cooperative and for insurance premiums for loans secured by condominium units, where the condominium association has an obligation to the unit owners to maintain a master policy insuring all condominium units.

[9] A conforming loan is a loan with a principal obligation at consummation that does not exceed the limit in effect as of the date the transaction's interest rate is set for the maximum principal obligation eligible for purchase by Freddie Mac.

[10] A jumbo loan is a loan with a principal obligation at consummation that exceeds the limit in effect as of the date the transaction's interest rate is set for the maximum principal obligation eligible for purchase by Freddie Mac.

B. Revisions to current exemptions.

The final rule expands the condominium-unit exemption to cover insurance premiums for loans secured by dwellings in condominiums, planned unit developments, or other common-interest communities in which dwelling ownership requires participation in a governing association, where the governing association has an obligation to the dwelling owners to maintain a master policy insuring all dwellings.

C. New exemptions.

The final rule also contains four new exemptions to the escrow requirement for:

1. Transactions to finance the initial construction of a dwelling;
2. Temporary or “bridge” loans with a loan term of twelve months or less;
3. Reverse-mortgage transactions; and
4. Small creditors that meet the following criteria:
   a. The creditor made more than 50% of its first-lien mortgages in rural or underserved areas during the preceding calendar year;
   b. The creditor had total assets of less than $2 billion at the end of the preceding calendar year (adjusted annually for inflation);
   c. The creditor and its affiliates originated 500 or fewer first-lien consumer credit transactions secured by a dwelling during the preceding calendar year; and
   d. Neither the creditor nor its affiliate maintains an escrow account for any consumer credit transaction secured by real property or a dwelling that it or its affiliate currently services, except for escrow accounts established for first-lien higher-priced mortgage loans between April 1, 2010, and June 1, 2013, or established after consummation as an accommodation to distressed consumers to assist such consumers in avoiding default or foreclosure.

   Notwithstanding the small-creditor exemption, a small creditor must establish an escrow account for any first-lien higher-priced mortgage loan if, at consummation, the loan is subject to a forward commitment to be purchased by an investor that does not itself qualify for the exemption.

D. Clarifications.

On May 23, 2013, the CFPB adopted amendments to clarify how to determine whether a county is considered “rural” and “underserved” for purposes of the small creditor exemption to the escrow requirements and other regulatory provisions. The amendments specifically clarify that a county’s “rural” and “underserved” status may be determined based on currently applicable Urban Influence Codes established by the United States Department of Agriculture, Economic Research Services (for “rural”) or based on Home Mortgage Disclosure Act data (for “underserved”). Illustrations are provided.

In connection with the amendments, the Bureau posts on its public web site a final list of rural and underserved counties, which is identical to a March 12, 2013 list, for use with mortgages consummated from

June 1, 2013, through December 31, 2013. The Bureau will post the list for use in 2014 when the relevant data become available.

The amendments also restore, on a temporary basis, certain existing protections relating to the ability-to-repay and prepayment penalties for high-priced mortgage loans until similar provisions under the Dodd-Frank take effect in January 2014.

Appraisals for Higher-Priced Mortgage Loans

Effective date: January 18, 2014

I. Overview

The final rules prohibit a creditor from extending a "higher-priced mortgage loan" to a consumer without obtaining, prior to consummation, a written appraisal of the property to be mortgaged performed by a certified or licensed appraiser who conducts a physical inspection of the interior of the property that will secure the transaction. The final rule requires creditors to obtain an appraisal or appraisals meeting certain specified standards, provide applicants with a notification regarding the use of the appraisals, and give applicants a copy of the written appraisals used.

The final rules were adopted on an interagency basis by the Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, National Credit Union Administration, CFPB, and the Federal Housing Finance Agency.

II. Scope

The final rules apply to "higher-priced mortgage loans."

For purposes of the rules, the term **"higher-priced mortgage loan"** means a closed-end consumer credit transaction secured by the consumer's principal dwelling with an APR that exceeds the average prime offer rate (APOR) by:

- 1.5 or more percentage points for first-lien conforming loans;[11]
- 2.5 or more percentage points for first-lien jumbo loans;[12] or
- 3.5 or more percentage points for subordinate-lien loans.

The **"average prime offer rate"** means an APR that is "derived from average interest rates, points, and other loan pricing terms currently offered to consumers by a representative sample of creditors for mortgage transactions that have low-risk pricing characteristics."

[11] A conforming loan is a loan with a principal obligation at consummation that does not exceed the limit in effect as of the date the transaction's interest rate is set for the maximum principal obligation eligible for purchase by Freddie Mac.

[12] A jumbo loan is a loan with a principal obligation at consummation that exceeds the limit in effect as of the date the transaction's interest rate is set for the maximum principal obligation eligible for purchase by Freddie Mac.

III. Exemptions

The final rules do not apply to the following types of transactions:

- Qualified mortgages, as defined in Section 1026.43(e);
- Transactions secured by a new manufactured home;
- Transactions secured by a mobile home, boat, or trailer;
- Transactions to finance the initial construction of a dwelling;
- Temporary bridge loans with maturity of 12 months or less; and
- Reverse-mortgage transactions.

The exemption for qualified mortgages may significantly limit the circumstances under which the new appraisal rules will apply. Most creditors that make subprime, or higher-priced, conforming mortgage loans are likely to do so only if the loan is a qualified mortgage, in order to avail themselves of the rebuttable presumption of compliance with the ability-to-repay rules.

IV. Appraisal Requirements for Higher-Priced Mortgage Loans

A. General rule

A creditor is prohibited from extending a higher-priced mortgage loan to a consumer without obtaining, prior to consummation, a written appraisal of the property to be mortgaged performed by a certified or licensed appraiser who conducts a physical inspection of the interior of the property that will secure the transaction.

B. Safe harbor

A creditor obtains a written appraisal that meets the requirements of the general rule if the creditor:

1. Orders that the appraiser perform the appraisal in conformity with the Uniform Standards of Professional Appraisal Practice and title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989;
2. Verifies through the National Registry that the appraiser who signed the appraiser's certification was a certified or licensed appraiser in the state in which the appraised property is located as of the date the appraiser signed the appraiser's certification;
3. Has no actual knowledge contrary to the facts or certifications contained in the written appraisal; and
4. Confirms that the written appraisal:
   a. Identifies the creditor who ordered the appraisal and the property and the interest being appraised;
   b. Indicates whether the contract price was analyzed;
   c. Addresses conditions in the property's neighborhood;
   d. Addresses the condition of the property and any improvements to the property;

- **e.** Indicates which valuation approaches were used and includes reconciliation if more than one valuation approach was used;
- **f.** Provides an opinion of the property's market value and an effective date for the opinion;
- **g.** Indicates that a physical inspection of the interior of the property was performed;
- **h.** Includes a certification signed by the appraiser that the appraisal was prepared in accordance with the requirements of the Uniform Standards of Professional Appraisal Practice; and
- **i.** Includes a certification signed by the appraiser that the appraisal was prepared in accordance with the requirements of title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989, and any implementing regulations.

C. Requirement to obtain a second appraisal where "flipping" may be involved

1. **General.** For certain transactions where the seller may be "flipping" a property, a creditor is prohibited from extending a higher-priced mortgage loan to a consumer for the acquisition of a principal dwelling without obtaining, prior to consummation, two written appraisals of the property to be mortgaged performed by two different certified or licensed appraisers who each conduct a physical inspection of the interior of the property that will secure the transaction. Two written appraisals are required where:
   - **a.** The seller acquired the property 90 or fewer days prior to the date of the consumer's agreement to acquire the property and the price in the consumer's agreement to acquire the property exceeds the seller's acquisition price by more than 10%; or
   - **b.** The seller acquired the property 91 to 180 days prior to the date of the consumer's agreement to acquire the property and the price in the consumer's agreement to acquire the property exceeds the seller's acquisition price by more than 20%.
2. **Special requirements for the second appraisal.** One of the two required appraisals generally must include an analysis of:
   - **a.** The difference between the price at which the seller acquired the property and the price that the consumer is obligated to pay to acquire the property under the agreement with the seller;
   - **b.** Changes in market conditions between the date the seller acquired the property and the date of the consumer's agreement to acquire the property; and
   - **c.** Any improvements made to the property between the date the seller acquired the property and the date of the consumer's agreement to acquire the property. [13]
3. **Exemptions from the second appraisal requirement.** The requirement to obtain a second appraisal does not apply to extensions of credit that finance a consumer's acquisition of property:

[13] If a creditor cannot determine the prior date of sale or sale price after exercising reasonable diligence, the second appraisal must include an analysis of the factors only to the extent that necessary information can be determined.

a. From a local, state, or federal government agency;

b. From a person who acquired title to the property through foreclosure, deed in lieu of foreclosure, or other similar judicial or non-judicial procedure as a result of the person's exercise of rights as the holder of a defaulted mortgage loan;

c. From a non-profit entity as part of a local, state, or federal government program under which the non-profit entity is permitted to acquire title to single-family properties for resale from a seller who acquired title to the property through the process of foreclosure, deed in lieu of foreclosure, or other similar judicial or non-judicial procedure;

d. From a person who acquired title to the property by inheritance or pursuant to a court order of dissolution of marriage, civil union, or domestic partnership, or of partition of joint or marital assets to which the seller was a party;

e. From an employer or relocation agency in connection with the relocation of an employee;

f. From a servicemember who received a deployment or permanent change of station order after the servicemember purchased the property;

g. Located in an area designated by the president as a federal disaster area or located in a rural county.

D. Charges

The final rules prohibit a creditor from charging the consumer for providing a copy of a written appraisal to the consumer, including by imposing a fee specifically for a required copy of an appraisal or by marking up the interest rate or any other fees payable by the consumer in connection with the higher-priced mortgage loan. This prohibition applies to copies of both the first and second appraisals.

The creditor may, however, charge the consumer for the cost of appraisal itself. If, however, the creditor must obtain two appraisals, the creditor may charge the consumer for one of the two appraisals.

V. Disclosure Requirements for Higher-Priced Mortgage Loan Appraisals

A creditor must provide a written disclosure to a consumer who applies for a higher-priced mortgage loan. The disclosure must state that an appraisal may be ordered and the consumer charged for the appraisal, that the creditor will provide the applicant a copy of any written appraisal even if the loan does not close, and that the consumer may choose to have a separate appraisal conducted for his or her own use at the consumer's own expense.

The creditor must place in the mail or deliver the disclosure no later than the third business day after the creditor receives an application for a higher-priced mortgage loan. If the loan is not a higher-priced mortgage loan at the time of application, but subsequently becomes a higher-priced mortgage loan, the disclosure must be placed in the mail or delivered not later than the third business day after the creditor determines that the loan is a higher-priced mortgage loan.

A creditor must provide to the consumer a copy of each written appraisal prepared in accordance with this provision in writing, or electronically with the consumer's consent, no later than:

- Three business days prior to consummation of the loan, or
- Thirty days after the creditor determines that the loan will not be consummated. [14]

[14] If two or more consumers apply for a higher-priced mortgage loan, the written disclosures about appraisals and the copies of the appraisals may be given to one of the consumers.

Disclosure and Delivery Requirements for Copies of Appraisals and Other Written Valuations

Effective date: January 18, 2014

I. Overview

The final rule amends Regulation B (Equal Credit Opportunity Act) to require creditors to provide applicants with a copy of appraisals and other written valuations developed in connection with an application for credit secured by a first lien on a dwelling without charge. The final rule also requires creditors to notify applicants in writing of their right to receive copies of appraisals developed.

II. Scope

The amended provision covers applications for credit to be secured by a first lien on a dwelling. This includes both closed-end and open-end credit. The rules apply regardless of whether credit is extended or denied or whether the application is incomplete or withdrawn.

III. Requirement to provide copies of appraisals and other valuations

A. General rule

A creditor must provide an applicant a copy of all appraisals and other written valuations developed in connection with an application for credit that is to be secured by a first lien on a dwelling. The copies must be provided promptly upon completion of each appraisal or written valuation, or three business days before consummation (for closed-end credit) or account opening (for open-end credit), whichever is earlier.

If there is more than one applicant, the written disclosure about written appraisals, and the copies of appraisals and other written valuations, need only be given to one applicant. However, these materials must be given to the primary applicant where one is readily apparent.

B. Waiver of timing requirement for disclosure

An applicant may waive the timing requirement for the creditor to provide a copy of the appraisal and other written valuation, and may agree to receive any copy at or before consummation or account opening, unless otherwise prohibited by law. Any such waiver must be obtained at least three business days prior to consummation or account opening, unless the waiver pertains solely to receipt of a copy of an appraisal or written valuation that contains only clerical changes from a previous version provided to the application within the applicable timeframes. If the transaction is not consummated or the account is not opened, the creditor must provide a copy no later than 30 days after the creditor determines the transaction will not be consummated or the account will not be opened.

C. Limits on charges

A creditor is prohibited from charging an applicant for providing a copy of the appraisals and other written valuations. This prohibition applies to charges for photocopy, postage, or other costs incurred in providing a copy of an appraisal or other written valuation.

However, the creditor may require applicants to pay a reasonable fee to reimburse the creditor for the cost of the appraisal or other written valuation, unless otherwise prohibited by law.

IV. Disclosure of right to receive copies of appraisals

A creditor must mail or deliver to an applicant, no later than the third business day after the creditor receives an application for credit that is to be secured by a first lien on a dwelling, a written notice of the applicant's right to receive a copy of all written appraisals developed in connection with the application. If an application for credit is not to be secured by a first lien on a dwelling at the time of the application, but the creditor later determines that the credit will be secured by a first lien on a dwelling, the creditor must mail or deliver the notice to the applicant no later than the third business day after the creditor determines that the loan is to be secured by a first lien on a dwelling.[15]

[15] If there is more than one applicant, the written disclosure about appraisals and the copies of the appraisals and other written valuations, may be given to one applicant, but must be given to the primary applicant where one is readily apparent.

Loan-Originator Compensation Requirements

Effective date: June 1, 2013, for prohibition on mandatory arbitration and prohibition on single-premium credit insurance; January 10, 2014, for other provisions.

I. Overview

The final rule on loan-originator compensation revises and expands upon existing Regulation Z (Truth in Lending) requirements regarding loan-originator qualification requirements and loan-originator compensation. The rules also prohibit mandatory arbitration agreements in consumer credit transactions secured by a dwelling, waivers of consumers' legal rights, and the financing of certain credit insurance in connection with a mortgage loan.[16]

The rules define a "loan originator" as a person who, for or in expectation of direct or indirect compensation or other monetary gain, performs any of the following activities: (1) "takes an application, offers, arranges, assists a consumer in obtaining or applying to obtain, negotiates, or otherwise obtains or makes an extension of credit for another person";[17] or (2) represents to the public through advertising or other means that such a person can or will perform any of these activities. A "loan originator" includes individuals and organizations, as well as an employee, agent, or contractor of the creditor or loan-originator organization. A loan originator may include an independent mortgage broker or a bank loan officer.[18]

II. Loan-Originator Compensation

A. Prohibition against compensation based on term of a transaction or proxies

1. **General prohibition.** No loan originator is permitted to receive and no person is permitted to pay to a loan originator, directly or indirectly, compensation in an amount based on a term of a transaction, the terms of multiple transactions by an individual loan originator, or the terms of multiple transactions by multiple individual loan originators. For purposes of the rule, a "term of a transaction" means "any right or obligation of the parties to a credit transaction."

   Example: A loan officer for a mortgage broker cannot receive compensation based on the interest rate of a loan or on the fact that the loan officer steered a consumer to purchase

[16] The final rule makes no changes to the prohibition against a loan originator's steering a consumer to a loan that will yield greater compensation to the originator.

[17] The language in (1) is taken verbatim from the final rule, but its meaning is not entirely clear, and a technical correction to the definition may be necessary. TILA section 103(cc)(2) defines the term "mortgage originator" to mean any person who for direct or indirect compensation or gain, or in the expectation of direct or indirect compensation or gain: (a) takes a residential mortgage-loan application; (2) assists a consumer in obtaining or applying to obtain a residential mortgage loan; or (3) offers or negotiates terms of a residential mortgage loan.

[18] A loan originator does not include seller financers subject to certain conditions. The conditions vary depending upon whether the seller financer provides financing for one property or three or fewer properties.

required title insurance from an affiliate of the broker, since the consumer is obligated to pay interest and the required title insurance in connection with the loan.

To prevent evasion, the rule generally prohibits loan-originator compensation from being reduced to offset the cost of a change in transaction terms (often called a “pricing concession”). However, the rule allows loan originators to reduce their compensation to defray certain unexpected increases in estimated settlement costs.

2. **Proxies.**
   a. If a loan originator’s compensation is based in whole or in part on a factor that is a proxy for a term of a transaction, the loan originator’s compensation is based on a term of a transaction.
   b. A factor that is not itself a term of a transaction is a proxy for a term of the transaction if the factor consistently varies with that term over a significant number of transactions and the loan originator has the ability, directly or indirectly, to add, drop, or change the factor in originating the transaction.

3. **Items that are not a “term of a transaction.”**
   a. Compensation based on the consumer’s credit score or similar representation of credit risk, such as the consumer’s debt-to income ratio, is not a term of a transaction. However, as noted above, if compensation varies in whole or in part with a factor that serves as a proxy for transaction terms or conditions, the compensation is deemed to be based on the terms of a transaction.
   b. The amount of credit extended is not a term of a transaction or a proxy for a term of a transaction, provided that compensation received by or paid to a loan originator, directly or indirectly, is based on a fixed percentage of the amount of credit extended. This form of compensation may be subject to a minimum or maximum dollar amount.
   c. Compensation in the form of a contribution to a tax-advantaged defined contribution or defined benefit plan is permitted and not a term of a transaction, as long as such contribution is not based on the terms of that individual loan originator’s transactions.
   d. Compensation under a non-deferred profits-based compensation plan is permitted and not a term of a transaction, as long as the compensation is not directly or indirectly based on the terms of that individual loan originator’s transactions and either:
      - The compensation, in the aggregate, does not exceed 10% of the individual loan originator’s total compensation; or
      - The individual was a loan originator for ten or fewer transactions consummated during the 12-month period preceding the date of the compensation determination.

B. Prohibition against dual compensation

The final rule retains the current prohibition against dual compensation. Specifically, if any loan originator receives compensation directly from a consumer in a consumer credit transaction secured by a dwelling:

- No loan originator shall receive compensation, directly or indirectly, from any person other than the consumer in connection with the transaction; and
- No person who knows or has reason to know of the consumer-paid compensation to the loan originator (other than the consumer) shall pay any compensation to a loan originator, directly or indirectly, in connection with the transaction.

The final rule clarifies that compensation received directly from a consumer includes payments to a loan originator made pursuant to an agreement between the consumer and a person other than the creditor or its affiliates, under which such other person agrees to provide funds toward the consumer's costs of the transaction (including loan originator compensation).

In addition, the final rule permits a loan-originator organization to pay compensation to its individual loan-originator employees or contractors, although the compensation cannot be based on the terms of the loans that they originate.

C. No prohibition on consumer payment of upfront points and fees

The final rule does not incorporate a proposed waiver of the ban on charging upfront points and fees in connection with a mortgage loan, provided that the creditor made available to consumers an alternative loan that did not include upfront points and fees. Instead, the final rule contains a complete exemption from the ban, pending further testing and research.

D. Recordkeeping

The rule contains revised recordkeeping requirements concerning loan-originator compensation that apply to both creditors and mortgage brokers. A creditor is required to maintain records sufficient to evidence all compensation it pays to a loan originator, and the compensation agreement that governs those payments, for three years after the date of payment. A loan-originator organization is required to maintain records sufficient to evidence all compensation it receives from a creditor, a consumer, or another person; all compensation it pays to any individual loan originator; and the compensation agreement that governs each receipt or payment, for three years after the date of each such receipt or payment.

III. Loan-Originator Qualifications

A. A loan originator for a consumer credit transaction secured by a dwelling must be "qualified" and, when applicable, registered or licensed to the extent required under state or federal law, including the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act) and state SAFE Act laws. To comply with this requirement, a loan-originator organization that is not a government agency or state housing finance agency must:

1. Comply with all applicable state requirements for legal existence and foreign qualification;

2. Ensure that each individual loan originator who works for the organization is licensed or registered to the extent the individual is required to be licensed or registered under the SAFE Act, its implementing regulations, and state SAFE Act law; and
3. For each of its individual loan-originator employees who is not required to be licensed and is not licensed as a loan originator, the organization must obtain:
    a. A criminal background check from a law enforcement agency for any individual whom the loan-originator organization hired on or after January 10, 2014;
    b. A credit report from a consumer reporting agency; and
    c. Information about any administrative, civil, or criminal findings against the individual loan originator from the Nationwide Mortgage Licensing System and Registry (NMLSR) for registered originators or from another source for unregistered originators.

B. For each of its individual loan-originator employees who is not required to be licensed and is not licensed as a loan originator, the organization must determine based on the information obtained or other information reasonably available to the organization that the individual loan originator:
1. Has not been convicted of, pleaded guilty or no contest to, a felony in a domestic or military court during the preceding seven years;
2. Has not been convicted of, pleaded guilty or no contest to, a felony involving an act of fraud, dishonesty, breach of trust, or money laundering, at any time; and
3. Has demonstrated financial responsibility, character, and general fitness, so as to justify a determination that the individual loan originator will operate honestly, fairly, and efficiently.

C. For each of its individual loan-originator employees who is not required to be licensed and is not licensed as a loan originator, the organization must provide periodic training covering federal and state law requirements that apply to the individual loan originator’s loan-origination activities.

IV. Loan-Document-Identifier Requirements

For a consumer credit transaction secured by a dwelling, a loan-originator organization must include the following information on the credit application, the note or loan contract, and the security instrument, whenever each such loan document is provided to a consumer or presented to a consumer for signature, as applicable:

- Its name and NMLSR ID, if the NMLSR has provided it an NMLSR ID. NMLSR ID means a number assigned by the Nationwide Mortgage Licensing System and Registry to facilitate electronic tracking and uniform identification of loan originators; and
- The name of the individual loan originator (as it appears in the NMLSR) with primary responsibility for the origination and, if the NMLSR has provided such person an NMLSR ID, that NMLSR ID.

The rule also provides a placeholder in anticipation that this information will also be required on the combined TILA/RESPA disclosure form once final rules adopting that form have been issued.

V. Prohibition on Mandatory-Arbitration Clauses and Waivers of Consumer Rights

The rule prohibits a contract or other agreement for a consumer credit transaction secured by a dwelling (including a home-equity line of credit secured by the consumer's principal dwelling) from including terms that require arbitration or any other non-judicial procedure to resolve any controversy or settle any claims arising out of the transaction.

The rule also prohibits a contract or other agreement for a consumer credit transaction secured by a dwelling (including a home-equity line of credit secured by the consumer's principal dwelling) from being applied or interpreted to bar a consumer from bringing a claim in court pursuant to any provision of law for damages or other relief in connection with any alleged violation of any federal law.

These prohibitions do not limit a consumer and creditor or any assignee from agreeing, after a dispute or claim under the transaction arises, to settle, use arbitration or other non-judicial procedures to resolve that dispute or claim.

VI. Prohibition on Financing Single-Premium Credit Insurance

A creditor may not finance, directly or indirectly, any premiums or fees for credit insurance in connection with a consumer credit transaction secured by a dwelling (including a home-equity line of credit secured by the consumer's principal dwelling).[19] This prohibition does not apply to credit insurance for which premiums or fees are calculated and paid in full on a monthly basis.

VII. Policies and Procedures to Ensure and Monitor Compliance

A depository institution must establish and maintain written policies and procedures reasonably designed to ensure and monitor the compliance of the depository institution, its employees, its subsidiaries, and its subsidiaries' employees with the requirements relating to loan-originator compensation, loan-originator qualifications, and loan-document identifiers. These written policies and procedures must be appropriate to the nature, size, complexity, and scope of the mortgage-lending activities of the depository institution and its subsidiaries.

[19] "Credit insurance" means credit life insurance; credit disability insurance; credit unemployment insurance; credit property insurance; any other accident, loss-of-income, life, or health insurance; or any payments for any debt cancellation, suspension agreement or contract. It excludes credit unemployment insurance in instances where the unemployment insurance premiums are reasonable, the creditor receives no direct or indirect compensation in connection with the unemployment insurance premiums, and the unemployment insurance premiums are paid pursuant to a separate insurance contract and are not paid to an affiliate of the creditor.

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