Regulation Z
Real Estate General

Reg Z University

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Indiana Bankers Association

Ohio Bankers League

Consultants to the Financial Industry
Young & Associates, Inc.
121 E. Main Street
P.O. Box 711
Kent, OH 44240
Phone: 330.678.0524
Fax: 330.678.6219
www.younginc.com

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Refinancing - 12 C.F.R § 1026.20(a)

Regulatory Discussion

This section includes the disclosure requirements in the event of a "refinancing."

Generally, a refinancing constitutes satisfaction (pay-off) of an existing obligation and replaced by a new obligation by the same consumer (borrower(s)). The commentary provides a definition of "refinancing" as well as discussion on variable rates and unearned finance charges.

A *renewal* of an existing obligation *is not a refinancing*. There are four other transactions that are also excluded as a refinancing. The commentary provides additional information on these five exclusions.

Regulatory Text

(a) **Refinancings.** A refinancing occurs when an existing obligation that was subject to this subpart is satisfied and replaced by a new obligation undertaken by the same consumer. A refinancing is a new transaction requiring new disclosures to the consumer. The new finance charge shall include any unearned portion of the old finance charge that is not credited to the existing obligation. The following shall not be treated as a refinancing:

(1) A renewal of a single payment obligation with no change in the original terms.

(2) A reduction in the annual percentage rate with a corresponding change in the payment schedule.

(3) An agreement involving a court proceeding.

(4) A change in the payment schedule or a change in collateral requirements as a result of the consumer's default or delinquency, unless the rate is increased, or the new amount financed exceeds the unpaid balance plus earned finance charge and premiums for continuation of insurance of the types described in §1026.4(d).

(5) The renewal of optional insurance purchased by the consumer and added to an existing transaction, if disclosures relating to the initial purchase were provided as required by this subpart.

Regulatory Commentary

20(a) Refinancings

1. ***Definition***. *A refinancing is a new transaction requiring a complete new set of disclosures. Whether a refinancing has occurred is determined by reference to whether the original obligation has been satisfied or extinguished and replaced by a new obligation, based on the parties' contract and applicable law. The refinancing may involve the consolidation of several existing obligations, disbursement of new money to the consumer or on the consumer's behalf, or the rescheduling of payments under an existing obligation. In any form, the new obligation must completely replace the prior one.*

   i. *Changes in the terms of an existing obligation, such as the deferral of individual installments, will not constitute a refinancing unless accomplished by the cancellation of that obligation and the substitution of a new obligation.*

   ii. *A substitution of agreements that meets the refinancing definition will require new disclosures, even if the substitution does not substantially alter the prior credit terms.*

2. ***Exceptions.*** *A transaction is subject to §1026.20(a) only if it meets the general definition of a refinancing. Section 1026.20(a)(1) through (5) lists 5 events that are not treated as refinancings, even if they are accomplished by cancellation of the old obligation and substitution of a new one.*

3. ***Variable-rate.***

   i. *If a variable-rate feature was properly disclosed under the regulation, a rate change in accord with those disclosures is not a refinancing. For example, no new disclosures are required when the variable-rate feature is invoked on a renewable balloon-payment mortgage that was previously disclosed as a variable-rate transaction.*

   ii. *Even if it is not accomplished by the cancellation of the old obligation and substitution of a new one, a new transaction subject to new disclosures results if the creditor either:*

      A. *Increases the rate based on a variable-rate feature that was not previously disclosed; or*

      B. *Adds a variable-rate feature to the obligation. A creditor does not add a variable-rate feature by changing the index of a variable-rate transaction to a comparable index, whether the change replaces the existing index or substitutes an index for one that no longer exists.*

   iii. *If either of the events in paragraph 20(a)-3.ii.A or ii.B occurs in a transaction secured by a principal dwelling with a term longer than one year, the disclosures required under §1026.19(b) also must be given at that time.*

4. ***Unearned finance charge.*** *In a transaction involving precomputed finance charges, the*

creditor must include in the finance charge on the refinanced obligation any unearned portion of the original finance charge that is not rebated to the consumer or credited against the underlying obligation. For example, in a transaction with an add-on finance charge, a creditor advances new money to a consumer in a fashion that extinguishes the original obligation and replaces it with a new one. The creditor neither refunds the unearned finance charge on the original obligation to the consumer nor credits it to the remaining balance on the old obligation. Under these circumstances, the unearned finance charge must be included in the finance charge on the new obligation and reflected in the annual percentage rate disclosed on refinancing. Accrued but unpaid finance charges are included in the amount financed in the new obligation.

5. ***Coverage.*** *Section 1026.20(a) applies only to refinancings undertaken by the original creditor or a holder or servicer of the original obligation. A "refinancing" by any other person is a new transaction under the regulation, not a refinancing under this section.*

Paragraph 20(a)(1)

1. ***Renewal.*** *This exception applies both to obligations with a single payment of principal and interest and to obligations with periodic payments of interest and a final payment of principal. In determining whether a new obligation replacing an old one is a renewal of the original terms or a refinancing, the creditor may consider it a renewal even if:*

   i. Accrued unpaid interest is added to the principal balance.

   ii. Changes are made in the terms of renewal resulting from the factors listed in §1026.17(c)(3).

   iii. The principal at renewal is reduced by a curtailment of the obligation.

Paragraph 20(a)(2)

1. ***Annual percentage rate reduction.*** *A reduction in the annual percentage rate with a corresponding change in the payment schedule is not a refinancing. If the annual percentage rate is subsequently increased (even though it remains below its original level) and the increase is effected in such a way that the old obligation is satisfied and replaced, new disclosures must then be made.*

2. ***Corresponding change.*** *A corresponding change in the payment schedule to implement a lower annual percentage rate would be a shortening of the maturity, or a reduction in the payment amount or the number of payments of an obligation. The exception in §1026.20(a)(2) does not apply if the maturity is lengthened, or if the payment amount or number of payments is increased beyond that remaining on the existing transaction.*

Paragraph 20(a)(3)

1. ***Court agreements.*** *This exception includes, for example, agreements such as reaffirmations of debts discharged in bankruptcy, settlement agreements, and post-judgment agreements. (See the commentary to §1026.2(a)(14) for a discussion of court-approved agreements that are not considered "credit.")*

Paragraph 20(a)(4)

1. ***Workout agreements.*** *A workout agreement is not a refinancing unless the annual percentage rate is increased or additional credit is advanced beyond amounts already accrued plus insurance premiums.*

Paragraph 20(a)(5)

1. ***Insurance renewal.*** *The renewal of optional insurance added to an existing credit transaction is not a refinancing, assuming that appropriate Truth in Lending disclosures were provided for the initial purchase of the insurance.*

Section 2: Assumptions
12 C.F.R. § 1026.20(b)

Assumptions - 12 C.F.R § 1026.20(b)

Regulatory Discussion

This section includes the disclosure requirements in the event of an "assumption."

Generally, an assumption occurs when a credit accepts a new consumer as replacement of the existing consumer as the primary obligor on an existing residential mortgage transaction. The commentary provides a definition of "assumption."

There are three conditions which must be met for a transaction to be considered an assumption:

- It must be a residential mortgage transaction
- There must be express acceptance of the new consumer by the creditor
- There must be a written agreement

See the commentary for additional information on these three conditions.

Regulatory Text

(b) **Assumptions.** An assumption occurs when a creditor expressly agrees in writing with a subsequent consumer to accept that consumer as a primary obligor on an existing residential mortgage transaction. Before the assumption occurs, the creditor shall make new disclosures to the subsequent consumer, based on the remaining obligation. If the finance charge originally imposed on the existing obligation was an add-on or discount finance charge, the creditor need only disclose:

(1) The unpaid balance of the obligation assumed.

(2) The total charges imposed by the creditor in connection with the assumption.

(3) The information required to be disclosed under §1026.18(k), (l), (m), and (n).

(4) The annual percentage rate originally imposed on the obligation.

(5) The payment schedule under §1026.18(g) and the total of payments under §1026.18(h) based on the remaining obligation.

Regulatory Commentary

20(b) Assumptions

*1. **General definition.***

i. An assumption as defined in §1026.20(b) is a new transaction and new disclosures must be made to the subsequent consumer. An assumption under the regulation requires the following three elements:

A. A residential mortgage transaction.

B. An express acceptance of the subsequent consumer by the creditor.

C. A written agreement.

ii. The assumption of a nonexempt consumer credit obligation requires no disclosures unless all three elements are present. For example, an automobile dealer need not provide Truth in Lending disclosures to a customer who assumes an existing obligation secured by an automobile. However, a residential mortgage transaction with the elements described in §1026.20(b) is an assumption that calls for new disclosures; the disclosures must be given whether or not the assumption is accompanied by changes in the terms of the obligation. (See comment 2(a)(24)-5 for a discussion of assumptions that are not considered residential mortgage transactions.)

*2. **Existing residential mortgage transaction.** A transaction may be a residential mortgage transaction as to one consumer and not to the other consumer. In that case, the creditor must look to the assuming consumer in determining whether a residential mortgage transaction exists. To illustrate: The original consumer obtained a mortgage to purchase a home for vacation purposes. The loan was not a residential mortgage transaction as to that consumer. The mortgage is assumed by a consumer who will use the home as a principal dwelling. As to that consumer, the loan is a residential mortgage transaction. For purposes of §1026.20(b), the assumed loan is an "existing residential mortgage transaction" requiring disclosures, if the other criteria for an assumption are met.*

*3. **Express agreement.** Expressly agrees means that the creditor's agreement must relate specifically to the new debtor and must unequivocally accept that debtor as a primary obligor. The following events are not construed to be express agreements between the creditor and the subsequent consumer:*

i. Approval of creditworthiness.

ii. Notification of a change in records.

iii. Mailing of a coupon book to the subsequent consumer.

iv. Acceptance of payments from the new consumer.

4. ***Retention of original consumer.*** *The retention of the original consumer as an obligor in some capacity does not prevent the change from being an assumption, provided the new consumer becomes a primary obligor. But the mere addition of a guarantor to an obligation for which the original consumer remains primarily liable does not give rise to an assumption. However, if neither party is designated as the primary obligor but the creditor accepts payment from the subsequent consumer, an assumption exists for purposes of §1026.20(b).*

5. ***Status of parties.*** *Section 1026.20(b) applies only if the previous debtor was a consumer and the obligation is assumed by another consumer. It does not apply, for example, when an individual takes over the obligation of a corporation.*

6. ***Disclosures****. For transactions that are assumptions within this provision, the creditor must make disclosures based on the "remaining obligation." For example:*

   i. *The amount financed is the remaining principal balance plus any arrearages or other accrued charges from the original transaction.*

   ii. *If the finance charge is computed from time to time by application of a percentage rate to an unpaid balance, in determining the amount of the finance charge and the annual percentage rate to be disclosed, the creditor should disregard any prepaid finance charges paid by the original obligor, but must include in the finance charge any prepaid finance charge imposed in connection with the assumption.*

   iii. *If the creditor requires the assuming consumer to pay any charges as a condition of the assumption, those sums are prepaid finance charges as to that consumer, unless exempt from the finance charge under §1026.4. If a transaction involves add-on or discount finance charges, the creditor may make abbreviated disclosures, as outlined in §1026.20(b)(1) through (5). Creditors providing disclosures pursuant to this section for assumptions of variable-rate transactions secured by the consumer's principal dwelling with a term longer than one year need not provide new disclosures under §1026.18(f)(2)(ii) or §1026.19(b). In such transactions, a creditor may disclose the variable-rate feature solely in accordance with §1026.18(f)(1).*

7. ***Abbreviated disclosures.*** *The abbreviated disclosures permitted for assumptions of transactions involving add-on or discount finance charges must be made clearly and conspicuously in writing in a form that the consumer may keep. However, the creditor need not comply with the segregation requirement of §1026.17(a)(1). The terms annual percentage rate and total of payments, when disclosed according to §1026.20(b)(4) and (5), are not subject to the description requirements of §1026.18(e) and (h). The term annual percentage rate disclosed under §1026.20(b)(4) need not be more conspicuous than other disclosures.*

Section 3: Rate and Payment Adjustments
12 C.F.R. § 1026.20(c)

Rate and Payment Adjustments - 12 C.F.R § 1026.20(c)

Regulatory Discussion

This section begins with the disclosure requirements in the event of rate and payment adjustments *on an adjustable rate mortgage* (ARM). There are three exemptions to this requirement.

Note: the requirements of this section also includes an interest rate adjustment resulting from conversion of an ARM to a fixed-rate transaction – if the rate adjustment results in a payment change.

There are fairly complex timing and content requirements.

Timing. Generally, the disclosures required by this section shall be provided at least 60, but no more than 120, days before the first payment at the adjusted level is due. There is an exception for ARMs originated prior to January 10, 2015

Content. The disclosures required by this section shall include seven pieces of information, as applicable.

Finally, the format of the disclosure must also meet specific requirements.

H-4(D)(2) Sample Form for § 1026.20(c)

July 20, 2012

Jordan and Dana Smith
4700 Jones Drive
Memphis, TN 38109

Springside Mortgage
1234 Main St
Memphis, TN 31801

Changes to Your Mortgage Interest Rate and Payments on September 1, 2012

Under the terms of your Adjustable-Rate Mortgage (ARM), you had a three-year period during which your interest rate stayed the same. That period ends on September 1, 2012, so on that date your interest rate and mortgage payment change. After that, your interest rate may change annually for the rest of your loan term.

	Current Rate and Monthly Payment	**New** Rate and Monthly Payment
Interest Rate	4.25%	6.25%
Total Monthly Payment	**$983.88**	**$1,211.81 (due October 1, 2012)**

Interest Rate: We calculated your interest rate by taking a published "index rate" and adding a certain number of percentage points, called the "margin." Under your loan agreement, your index rate is the 1-year LIBOR and your margin is 2.25%. The LIBOR index is published daily in the Wall Street Journal.

Rate Limits: Your rate cannot go higher than 11.625% over the life of the loan. Your rate can change each year by no more than 2.00%.

New Interest Rate and Monthly Payment: The table above shows your new interest rate and new monthly payment. Your new payment is based on the LIBOR index, your margin, your loan balance of $189,440, and your remaining loan term of 324 months.

Prepayment Penalty: Keep in mind that if you pay off your loan, refinance or sell your home before September 1, 2012, you could be charged a penalty. Contact Springside Mortgage at (800) 765-4321 for more information, such as the maximum amount of the penalty you could be charged.

Regulatory Text

(c) **Rate adjustments with a corresponding change in payment.** The creditor, assignee, or servicer of an adjustable-rate mortgage shall provide consumers with disclosures, as described in this paragraph (c), in connection with the adjustment of interest rates pursuant to the loan contract that results in a corresponding adjustment to the payment. To the extent that other provisions of this subpart C govern the disclosures required by this paragraph (c), those provisions apply to assignees and servicers as well as to creditors. The disclosures required by this paragraph (c) also shall be provided for an interest rate adjustment resulting from the conversion of an adjustable-rate mortgage to a fixed-rate transaction, if that interest rate adjustment results in a corresponding payment change.

(1) **Coverage**

(i) **In general.** For purposes of this paragraph (c), an adjustable-rate mortgage or "ARM" is a closed-end consumer credit transaction secured by the consumer's principal dwelling in which the annual percentage rate may increase after consummation.

(ii) **Exemptions.** The requirements of this paragraph (c) do not apply to:

(A) ARMs with terms of one year or less;

(B) The first interest rate adjustment to an ARM if the first payment at the adjusted level is due within 210 days after consummation and the new interest rate disclosed at consummation pursuant to §1026.20(d) was not an estimate; or

(C) The creditor, assignee or servicer of an adjustable-rate mortgage when the servicer on the loan is subject to the Fair Debt Collections Practices Act (FDCPA) (15 U.S.C. 1692 *et seq.*) with regard to the loan and the consumer has sent a notification pursuant to FDCPA section 805(c) (15 U.S.C. 1692c(c)).

(2) **Timing and content.** Except as otherwise provided in paragraph (c)(2) of this section, the disclosures required by this paragraph (c) shall be provided to consumers at least 60, but no more than 120, days before the first payment at the adjusted level is due. The disclosures shall be provided to consumers at least 25, but no more than 120, days before the first payment at the adjusted level is due for ARMs with uniformly scheduled interest rate adjustments occurring every 60 days or more frequently and for ARMs originated prior to January 10, 2015 in which the loan contract requires the adjusted interest rate and payment to be calculated based on the index figure available as of a date that is less than 45 days prior to the adjustment date. The disclosures shall be provided to consumers as soon as practicable, but not less than 25 days before the first payment at the adjusted level is due, for the first adjustment to an ARM if it occurs within 60 days of consummation and the new interest rate disclosed at consummation pursuant to §1026.20(d) was an estimate. The disclosures required by this paragraph (c) shall include:

(i) A statement providing:

(A) An explanation that under the terms of the consumer's adjustable-rate mortgage, the specific time period in which the current interest rate has been in effect is ending and the interest rate and mortgage payment will change;

(B) The effective date of the interest rate adjustment and when additional future interest rate adjustments are scheduled to occur; and

(C) Any other changes to loan terms, features, or options taking effect on the same date as the interest rate adjustment, such as the expiration of interest-only or payment-option features.

(ii) A table containing the following information:

(A) The current and new interest rates;

(B) The current and new payments and the date the first new payment is due; and

(C) For interest-only or negatively-amortizing payments, the amount of the current and new payment allocated to principal, interest, and taxes and insurance in escrow, as applicable. The current payment allocation disclosed shall be the payment allocation for the last payment prior to the date of the disclosure. The new payment allocation disclosed shall be the expected payment allocation for the first payment for which the new interest rate will apply.

(iii) An explanation of how the interest rate is determined, including:

(A) The specific index or formula used in making interest rate adjustments and a source of information about the index or formula; and

(B) The type and amount of any adjustment to the index, including any margin and an explanation that the margin is the addition of a certain number of percentage points to the index, and any application of previously foregone interest rate increases from past interest rate adjustments.

(iv) Any limits on the interest rate or payment increases at each interest rate adjustment and over the life of the loan, as applicable, including the extent to which such limits result in the creditor, assignee, or servicer foregoing any increase in the interest rate and the earliest date that such foregone interest rate increases may apply to future interest rate adjustments, subject to those limits.

(v) An explanation of how the new payment is determined, including:

(A) The index or formula used;

(B) Any adjustment to the index or formula, such as the addition of a margin or the application of any previously foregone interest rate increases from past interest rate adjustments;

(C) The loan balance expected on the date of the interest rate adjustment; and

(D) The length of the remaining loan term expected on the date of the interest rate adjustment and any change in the term of the loan caused by the adjustment.

(vi) If applicable, a statement that the new payment will not be allocated to pay loan principal and will not reduce the loan balance. If the new payment will result in negative amortization, a statement that the new payment will not be allocated to pay loan principal and will pay only part of the loan interest, thereby adding to the balance of the loan. If the new payment will result in negative amortization as a result of the interest rate adjustment, the statement shall set forth the payment required to amortize fully the remaining balance at the new interest rate over the remainder of the loan term.

(vii) The circumstances under which any prepayment penalty, as defined in §1026.32(b)(6)(i), may be imposed, such as when paying the loan in full or selling or refinancing the principal dwelling; the time period during which such a penalty may be imposed; and a statement that the consumer may contact the servicer for additional information, including the maximum amount of the penalty.

(3) **Format.**

(i) The disclosures required by this paragraph (c) shall be provided in the form of a table and in the same order as, and with headings and format substantially similar to, forms H-4(D)(1) and (2) in appendix H to this part; and

(ii) The disclosures required by paragraph (c)(2)(ii) of this section shall be in the form of a table located within the table described in paragraph (c)(3)(i) of this section. These disclosures shall appear in the same order as, and with headings and format substantially similar to, the table inside the larger table in forms H-4(D)(1) and (2) in appendix H to this part.

Regulatory Commentary

20(c) Rate adjustments with a corresponding change in payment.

*1. **Creditors, assignees, and servicers.** Creditors, assignees, and servicers that own either the applicable adjustable-rate mortgage or the applicable mortgage servicing rights or both are subject to the requirements of §1026.20(c). Creditors, assignees, and servicers are also subject to the requirements of any provision of subpart C that governs §1026.20(c). For example, the form requirements of §1026.17(a) apply to §1026.20(c) disclosures and thus, assignees and servicers, as well as creditors, are subject to those requirements. While creditors, assignees, and servicers are all subject to the requirements of §1026.20(c), they may decide among themselves which of them will provide the required disclosures.*

*2. **Loan modifications.** Under §1026.20(c), the interest rate adjustment disclosures are required only for interest rate adjustments occurring pursuant to the loan contract. Accordingly, creditors, assignees, and servicers need not provide the disclosures for interest rate adjustments occurring in loan modifications made for loss mitigation purposes. Subsequent interest rate adjustments resulting in a corresponding payment change occurring pursuant to the modified loan contract, however, are subject to the requirements of §1026.20(c).*

*3. **Conversions.** In addition to the disclosures required for interest rate adjustments under an adjustable-rate mortgage, §1026.20(c) also requires the disclosures for an ARM converting to a fixed-rate transaction when the conversion changes the interest rate and results in a corresponding payment change. When an open-end account converts to a closed-end adjustable-rate mortgage, the §1026.20(c) disclosure is not required until the implementation of an interest rate adjustment post-conversion that results in a corresponding payment change. For example, for an open-end account that converts to a closed-end 3/1 hybrid ARM, i.e., an ARM with a fixed rate of interest for the first three years after which the interest rate adjusts annually, the first §1026.20(c) disclosure would not be required until three years after the conversion, and only if that first adjustment resulted in a payment change.*

Paragraph 20(c)(1)(i).

1. ***In general.*** *An adjustable-rate mortgage, as defined in §1026.20(c)(1)(i), is a variable-rate transaction as that term is used in subpart C, except as distinguished by comment §1026.20(c)(1)(ii)-3. The requirements of this section are not limited to transactions financing the initial acquisition of the consumer's principal dwelling.*

Paragraph 20(c)(1)(ii).

1. ***Short-term ARMs.*** *Under §1026.20(c)(1)(ii), construction, home improvement, bridge, and other loans with terms of one year or less are not subject to the requirements in §1026.20(c). In determining the term of a construction loan that may be permanently financed by the same creditor or assignee, the creditor or assignee may treat the construction and the permanent phases as separate transactions with distinct terms to maturity or as a single combined transaction.*

2. ***First new payment due within 210 days after consummation.*** *Section 1026.20(c) disclosures are not required if the first payment at the adjusted level is due within 210 days after consummation, when the new interest rate disclosed at consummation pursuant to §1026.20(d) is not an estimate. For example, the creditor, assignee, or servicer would not be required to provide the disclosures required by §1026.20(c) for the first time an ARM interest rate adjusts if the first payment at the adjusted level was due 120 days after consummation and the adjusted interest rate disclosed at consummation pursuant to §1026.20(d) was not an estimate.*

3. ***Non-adjustable-rate mortgages.*** *The following transactions, if structured as fixed-rate and not as adjustable-rate mortgages based on an index or formula, are not subject to §1026.20(c):*

   i. Shared-equity or shared-appreciation mortgages;

   ii. Price-level adjusted or other indexed mortgages that have a fixed rate of interest but provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation;

   iii. Graduated-payment mortgages or step-rate transactions;

   iv. Renewable balloon-payment instruments; and

   v. Preferred-rate loans.

Paragraph 20(c)(2).

1. ***Timing.*** *The requirement that §1026.20(c) disclosures be provided to consumers within a certain timeframe means that the creditor, assignee, or servicer must deliver the notice or place it in the mail within that timeframe, excluding any grace or courtesy periods. The requirement that the §1026.20(c) disclosures must be provided between 25 and 120 days before the first payment at the adjusted level is due for frequently-adjusting ARMs, applies to ARMs that adjust regularly at a maximum of every 60 days.*

Paragraph 20(c)(2)(ii)(A).

1. ***Current and new interest rates.*** *The current interest rate is the interest rate that applies on the date the disclosure is provided to the consumer. The new interest rate is the actual interest rate that will apply on the date of the adjustment. The new interest rate is used to determine the new payment. The "new interest rate" has the same meaning as the "adjusted interest rate." The requirements of §1026.20(c)(2)(ii)(A) do not preclude creditors, assignees, and servicers from rounding the interest rate, pursuant to the requirements of the ARM contract.*

Paragraph 20(c)(2)(iv).

1. ***Rate limits and foregone interest rate increases.*** *Interest rate carryover, or foregone interest rate increases, is the amount of interest rate increase foregone at any ARM interest rate adjustment that, subject to rate caps, can be added to future interest rate adjustments to increase, or to offset decreases in, the rate determined by using the index or formula. The disclosures required by §1026.20(c)(2)(iv) regarding foregone interest rate increases apply only to transactions permitting interest rate carryover.*

Paragraph 20(c)(2)(v)(B).

1. ***Application of previously foregone interest rate increases.*** *The disclosures regarding the application of previously foregone interest rate increases apply only to transactions permitting interest rate carryover.*

Paragraph 20(c)(2)(vi).

1. ***Amortization statement.*** *For ARMs requiring the payment of interest only, such as interest-only loans, §1026.20(c)(2)(vi) requires a statement that the new payment covers all of the interest but none of the principal, and therefore will not reduce the loan balance. For negatively-amortizing ARMs, §1026.20(c)(2)(vi) requires a statement that the new payment covers only part of the interest and none of the principal, and therefore the unpaid interest will be added to the principal balance.*

2. ***Amortization payment.*** *Disclosure of the payment needed to amortize fully the outstanding balance at the new interest rate over the remainder of the loan term is required only when negative amortization occurs as a result of the interest rate adjustment. The disclosure is not required simply because a loan has interest-only or partially-amortizing payments. For example, an ARM with a five-year term and payments based on a longer amortization schedule, in which the final payment will equal the periodic payment plus the remaining unpaid balance, does not require disclosure of the payment necessary to amortize fully the loan in the remainder of the five-year term. A disclosure is also not required when the new payment is sufficient to prevent negative amortization but the final loan payment will be a different amount due to rounding.*

Paragraph 20(c)(2)(vii).

1. ***Prepayment penalty.*** *The creditor, assignee, or servicer of an ARM with no prepayment penalty, as that term is used in §1026.20(c)(2)(vii), may decide to exclude the prepayment section from the §1026.20(c) disclosure, retain the prepayment section and insert after the heading "None" or other indication that there is no prepayment penalty, or indicate there is no prepayment penalty in some other manner. See also comment 1.vi to Appendices G and H—Open-End and Closed-End Model Forms and Clauses.*

Paragraph 20(c)(3)(i).

1. ***Format of disclosures.*** *The requirements of §1026.20(c)(3)(i) and (ii) to provide the §1026.20(c) disclosures in the same order as, and with headings and format substantially similar to, the model and sample forms do not preclude creditors, assignees, and servicers from modifying the disclosures to accommodate particular consumer circumstances or transactions not addressed by the forms. For example, in the case of a consumer bankruptcy or under certain State laws, the creditor, assignee, or servicer may modify the forms to remove language regarding personal liability. Creditors, assignees, and servicers providing the required notice to a consumer whose ARM is converting to a fixed-rate mortgage, may modify the model language to explain that the interest rate will no longer adjust. Creditors, assignees, and servicers electing to provide consumers with interest rate notices in cases where the interest rate adjusts without a corresponding change in payment may modify the forms to fit that circumstance. A payment-option ARM, which is an ARM permitting consumers to choose among several different payment options for each billing period, is an example of a loan that may require modification of the §1026.20(c) model and sample forms. See appendix H-30(C) for an example of an allocation table for a payment-option loan.*

Section 4: Initial Rate Adjustment 12 C.F.R. § 1026.20(d)

Initial Rate Adjustment - 12 C.F.R § 1026.20(d)

Regulatory Discussion

This section begins with the disclosure requirements in connection with the initial rate adjustment *on an adjustable rate mortgage* (ARM); except for ARMs with a term of one year or less.

This disclosure must be provided separately from other documents

If the first payment at the adjusted level is due within the first 210 after consummation, this disclosure shall be provided at consummation; otherwise, this disclosure must be provide at least 210, but no more than 240, days before the first payment at the adjusted level is due.

Next, there are fairly complex content requirements. The disclosures required by this section shall include eleven pieces of information, as applicable.

Finally, the format of the disclosure must also meet specific requirements.

H-4(D)(3) Model Form for § 1026.20(d)

(Date)

Changes to Your Mortgage Interest Rate and Payments on *(date)*

Under the terms of your Adjustable-Rate Mortgage (ARM), you had a *(duration)* period during which your interest rate stayed the same. That period ends on *(date)*, so on that date your interest rate may change. After that, your interest rate may change *(frequency)* for the rest of your loan term. Any change in your interest rate may also change your mortgage payment. [Also, as of *(date) (change(s) to loan terms, features or options)*.]

	Current Rate and *(frequency)* Payment	[**Estimated**] **New** Rate and *(frequency)* Payment
Interest Rate	___%	___%
[Principal]	[$______]	[$______]
[Interest]	[$______]	[$______]
[Escrow (Taxes and Insurance)]	[$______]	[$______]
Total *(frequency)* Payment	**$______**	**$______ (due *(date)*)**

Interest Rate: We calculated your interest rate by taking a published "index rate" and adding a certain number of percentage points, called the "margin." Under your loan agreement, your index rate is *(index)* and your margin is ___%. The *(index)* is published *(frequency)* in *(source of information)*. [*Description and amount of other adjustment(s) to the index*.]

[**Rate Limit[s]**: [Your rate cannot go higher than ___% over the life of the loan.] [Your rate can change each year by no more than ___%.] [We did not include an additional ___% interest rate increase to your new rate because a rate limit applied. This additional increase may be applied to your interest rate when it adjusts again on *(date)*.]]

New Interest Rate and Monthly Payment: The table above shows [our estimate of] your new interest rate and new monthly payment. These amounts are based on the *(index)* as of now, your margin, [*description of other adjustment(s) to the index*,] your loan balance of $______, and your remaining loan term of ___ months. **[However, if the *(index)* has changed when we calculate the exact amount of your new interest rate and payment, your new interest rate and payment may be different from the estimate above. We will send you another notice with the exact amount of your new interest rate and payment 2 to 4 months before the first new payment is due, if your new payment will be different from your current payment.]**

[**Interest-Only Payments:** Your new payment will not cover any principal. Therefore, making this payment will not reduce your loan balance.]

[**Warning about Increase in Your Loan Balance:** Your new payment covers only part of the interest and no principal. Therefore, the unpaid interest will add to the balance of the loan. In order to fully pay off your loan by the end of the loan term at the new interest rate, you would have to pay $_____ per month.]]

[**Prepayment Penalty**: [None] [Keep in mind that if you pay off your loan, refinance or sell your home before *(date)*, you could be charged a penalty. Contact *(mortgage company)* at the telephone number [*or (email address)*] below for more information, such as the maximum amount of the penalty you could be charged.]]

If You Anticipate Problems Making Your Payments:

- Contact *(mortgage company)* at *(telephone number)* [or *(email address)*] as soon as possible.
- If you seek an alternative to the upcoming changes to your interest rate and payment, the following options **may** be possible (most are subject to lender approval):
  - Refinance your loan with us or another lender;
  - Sell your home and use the proceeds to pay off your current loan;
  - Modify your loan terms with us;
  - Payment forbearance temporarily gives you more time to pay your monthly payment.
- If you would like contact information for counseling agencies or programs in your area, call the U.S. Department of Housing and Urban Development (HUD) at (*telephone number*) or visit [*(internet address of the U.S. Department of Housing and Urban Development counseling agency list)* [or] [the U.S. Consumer Financial Protection Bureau (CFPB) at (*internet address of the U.S. Consumer Financial Protection Bureau homeownership counselors and counseling organization list)*]. If you would like contact information for a state housing finance agency, contact the U.S. Consumer Financial Protection Bureau (CFPB) at *(internet address of U.S. Consumer Financial Protection Bureau state housing finance agency access list)*.

Regulatory Text

(d) **Initial rate adjustment.** The creditor, assignee, or servicer of an adjustable-rate mortgage shall provide consumers with disclosures, as described in this paragraph (d), in connection with the initial interest rate adjustment pursuant to the loan contract. To the extent that other provisions of this subpart C govern the disclosures required by this paragraph (d), those provisions apply to assignees and servicers as well as to creditors. The disclosures required by this paragraph (d) shall be provided as a separate document from other documents provided by the creditor, assignee, or servicer. The disclosures shall be provided to consumers at least 210, but no more than 240, days before the first payment at the adjusted level is due. If the first payment at the adjusted level is due within the first 210 days after consummation, the disclosures shall be provided at consummation.

(1) **Coverage**

(i) **In general.** For purposes of this paragraph (d), an adjustable-rate mortgage or "ARM" is a closed-end consumer credit transaction secured by the consumer's principal dwelling in which the annual percentage rate may increase after consummation.

(ii) **Exemptions.** The requirements of this paragraph (d) do not apply to ARMs with terms of one year or less.

(2) **Content.** If the new interest rate (or the new payment calculated from the new interest rate) is not known as of the date of the disclosure, an estimate shall be disclosed and labeled as such. This estimate shall be based on the calculation of the index reported in the source of information described in paragraph (d)(2)(iv)(A) of this section within fifteen business days prior to the date of the disclosure. The disclosures required by this paragraph (d) shall include:

(i) The date of the disclosure.

(ii) A statement providing:

(A) An explanation that under the terms of the consumer's adjustable-rate mortgage, the specific time period in which the current interest rate has been in effect is ending and that any change in the interest rate may result in a change in the mortgage payment;

(B) The effective date of the interest rate adjustment and when additional future interest rate adjustments are scheduled to occur; and

(C) Any other changes to loan terms, features, or options taking effect on the same date as the interest rate adjustment, such as the expiration of interest-only or payment-option features.

(iii) A table containing the following information:

(A) The current and new interest rates;

(B) The current and new payments and the date the first new payment is due; and

(C) For interest-only or negatively-amortizing payments, the amount of the current and new payment allocated to principal, interest, and taxes and insurance in escrow, as applicable. The current payment allocation disclosed shall be the payment allocation for the last payment prior to the date of the disclosure. The new payment allocation disclosed shall be the expected payment allocation for the first payment for which the new interest rate will apply.

(iv) An explanation of how the interest rate is determined, including:

(A) The specific index or formula used in making interest rate adjustments and a source of information about the index or formula; and

(B) The type and amount of any adjustment to the index, including any margin and an explanation that the margin is the addition of a certain number of percentage points to the index.

(v) Any limits on the interest rate or payment increases at each interest rate adjustment and over the life of the loan, as applicable, including the extent to which such limits result in the creditor, assignee, or servicer foregoing any increase in the interest rate and the earliest date that such foregone interest rate increases may apply to future interest rate adjustments, subject to those limits.

(vi) An explanation of how the new payment is determined, including:

(A) The index or formula used;

(B) Any adjustment to the index or formula, such as the addition of a margin;

(C) The loan balance expected on the date of the interest rate adjustment;

(D) The length of the remaining loan term expected on the date of the interest rate adjustment and any change in the term of the loan caused by the adjustment; and

(E) If the new interest rate or new payment provided is an estimate, a statement that another disclosure containing the actual new interest rate and new payment will be provided to the consumer between two and four months before the first payment at the adjusted level is due for interest rate adjustments that result in a corresponding payment change.

(vii) If applicable, a statement that the new payment will not be allocated to pay loan principal and will not reduce the loan balance. If the new payment will result in negative amortization, a statement that the new payment will not be allocated to pay loan principal and will pay only part of the loan interest, thereby adding to the balance of the loan. If the new payment will result in negative amortization as a result of the interest rate adjustment, the statement shall set forth the payment required to amortize fully the remaining balance at the new interest rate over the remainder of the loan term.

(viii) The circumstances under which any prepayment penalty, as defined in §1026.32(b)(6)(i), may be imposed, such as when paying the loan in full or selling or refinancing the principal dwelling; the time period during which such a penalty may be imposed; and a statement that the consumer may contact the servicer for additional information, including the maximum amount of the penalty.

(ix) The telephone number of the creditor, assignee, or servicer for consumers to call if they anticipate not being able to make their new payments.

(x) The following alternatives to paying at the new rate that consumers may be able to pursue and a brief explanation of each alternative, expressed in simple and clear terms:

(A) Refinancing the loan with the current or another creditor or assignee;

(B) Selling the property and using the proceeds to pay the loan in full;

(C) Modifying the terms of the loan with the creditor, assignee, or servicer; and

(D) Arranging payment forbearance with the creditor, assignee, or servicer.

(xi) The Web site to access either the Bureau list or the HUD list of homeownership counselors and counseling organizations, the HUD toll-free telephone number to access the HUD list of homeownership counselors and counseling organizations, and the Bureau Web site to access contact information for State housing finance authorities (as defined in §1301 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989).

(3) **Format.**

(i) Except for the disclosures required by paragraph (d)(2)(i) of this section, the disclosures required by this paragraph (d) shall be provided in the form of a table and in the same order as, and with headings and format substantially similar to, forms H-4(D)(3) and (4) in appendix H to this part;

(ii) The disclosures required by paragraph (d)(2)(i) of this section shall appear outside of and above the table required in paragraph (d)(3)(i) of this section; and

(iii) The disclosures required by paragraph (d)(2)(iii) of this section shall be in the form of a table located within the table described in paragraph (d)(3)(i) of this section. These disclosures shall appear in the same order as, and with headings and format substantially similar to, the table inside the larger table in forms H-4(D)(3) and (4) in appendix H to this part.

Regulatory Commentary

20(d) Initial rate adjustment.

*1. **Creditors, assignees, and servicers.** Creditors, assignees, and servicers that own either the applicable adjustable-rate mortgage or the applicable mortgage servicing rights or both are subject to the requirements of §1026.20(d). Creditors, assignees, and servicers are also subject to the requirements of any provision of subpart C that governs §1026.20(d). For example, the form requirements of §1026.17(a) apply to §1026.20(d) disclosures and thus,* *assignees and servicers, as well as creditors, are subject to those requirements. While creditors, assignees, and servicers are all subject to the requirements of §1026.20(d), they may decide among themselves which of them will provide the required disclosures.*

*2. **Loan modifications.** Under §1026.20(d), the interest rate adjustment disclosures are required only for the initial interest rate adjustment occurring pursuant to the loan contract. Accordingly, creditors, assignees, and servicers need not provide the disclosures for interest rate adjustments occurring in loan modifications made for loss mitigation purposes. The initial interest rate adjustment occurring pursuant to the modified loan contract, however, is subject to the requirements of §1026.20(d).*

*3. **Timing and form of initial rate adjustment.** The requirement that §1026.20(d) disclosures be provided in writing, separate and distinct from all other correspondence, means that the initial ARM interest rate adjustment notice must be provided to consumers as a separate document but may, in the case of mailing the disclosure, be in the same envelope with other material and, in the case of emailing the disclosure, be a separate attachment from other attachments in the same email. The requirement that the disclosures be provided to consumers between 210 and 240 days "before the first payment at the adjusted level is due" means the creditor, assignee, or servicer must deliver the notice or place it in the mail between 210 and 240 days prior to the due date, excluding any grace or courtesy periods, of the first payment calculated using the adjusted interest rate.*

*4. **Conversions.** When an open-end account converts to a closed-end adjustable-rate mortgage, the §1026.20(d) disclosure is not required until the implementation of the initial interest rate adjustment post-conversion. For example, for an open-end account that converts to a closed-end 3/1 hybrid ARM, i.e., an ARM with a fixed rate of interest for the first three years after which the interest rate adjusts annually, the §1026.20(d) disclosure would not be required until three years after the conversion when the interest rate adjusts for the first time.*

Paragraph 20(d)(1)(i).

*1. **In general.** An adjustable-rate mortgage, as defined in §1026.20(d)(1)(i), is a variable-rate transaction as that term is used in subpart C, except as distinguished by comment §1026.20(d)(1)(ii)-2. The requirements of this section are not limited to transactions financing the initial acquisition of the consumer's principal dwelling.*

Paragraph 20(d)(1)(ii).

*1. **Short-term ARMs.** Under §1026.20(d)(1)(ii), construction, home improvement, bridge, and other loans with terms of one year or less are not subject to the requirements in §1026.20(d). In determining the term of a construction loan that may be permanently financed by the same creditor or assignee, the creditor or assignee may treat the construction and the permanent phases as separate transactions with distinct terms to maturity or as a single combined transaction.*

*2. **Non-adjustable-rate mortgages.** The following transactions, if structured as fixed-rate* *and not as adjustable-rate mortgages based on an index or formula, are not subject to §1026.20(d):*

i. Shared-equity or shared-appreciation mortgages;

ii. Price-level adjusted or other indexed mortgages that have a fixed rate of interest but provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation;

iii. Graduated-payment mortgages or step-rate transactions;

iv. Renewable balloon-payment instruments; and

v. Preferred-rate loans.

Paragraph 20(d)(2)(i).

*1. **Date of the disclosure.** The date that must appear on the disclosure is the date the creditor, assignee, or servicer generates the notice to be provided to the consumer.*

Paragraph 20(d)(2)(iii)(A).

*1. **Current and new interest rates.** The current interest rate is the interest rate that applies on the date of the disclosure. The new interest rate is the interest rate used to calculate the new payment and may be an estimate pursuant to §1026.20(d)(2). The new payment, if calculated from an estimated new interest rate, will also be an estimate. The "new interest rate" has the same meaning as the "adjusted interest rate." The requirements of §1026.20(d)(2)(iii)(A) do not preclude creditors, assignees, and servicers from rounding the interest rate, pursuant to the requirements of the ARM contract.*

Paragraph 20(d)(2)(v).

*1. **Rate limits and foregone interest rate increases.** Interest rate carryover, or foregone interest rate increases, is the amount of interest rate increase foregone at the first ARM interest rate adjustment that, subject to rate caps, can be added to future interest rate adjustments to increase, or to offset decreases in, the rate determined by using the index or formula. The disclosures required by §1026.20(d)(2)(v) regarding foregone interest rate increases apply only to transactions permitting interest rate carryover.*

Paragraph 20(d)(2)(vii).

*1. **Amortization statement.** For ARMs requiring the payment of interest only, such as interest-only loans, §1026.20(d)(2)(vii) requires a statement that the new payment covers all of the interest but none of the principal, and therefore will not reduce the loan balance. For negatively-amortizing ARMs, §1026.20(d)(2)(vii) requires a statement that the new payment covers only part of the interest and none of the principal, and therefore the unpaid interest will be added to the principal balance.*

*2. **Amortization payment.** Disclosure of the payment needed to amortize fully the outstanding balance at the new interest rate over the remainder of the loan term is required only when negative amortization occurs as a result of the interest rate adjustment. The disclosure is not required simply because a loan has interest-only or partially-amortizing payments. For example, an ARM with a five-year term and payments based on a longer amortization schedule, in which the final payment will equal the periodic payment plus the remaining unpaid balance, does not require disclosure of the payment necessary to amortize fully the loan in the remainder of the five-year term. A disclosure is also not required when the new payment is sufficient to prevent negative amortization but the final loan payment will be a different amount due to rounding.*

Paragraph 20(d)(2)(viii).

*1. **Prepayment penalty.** The creditor, assignee, or servicer of an ARM with no prepayment penalty, as that term is used in §1026.20(d)(2)(viii), may decide to exclude the prepayment section from the §1026.20(d) disclosure, retain the prepayment section and insert after the heading "None" or other indication that there is no prepayment penalty, or indicate there is no prepayment penalty in some other manner. See also comment to Appendices G and H - Open-End and Closed-End Model Forms and Clauses - 1.vi.*

Paragraph 20(d)(3)(i).

*1. **Format of disclosures.** The requirements of §1026.20(d)(3)(i) and (iii) to provide the §1026.20(d) disclosures in the same order as, and with headings and format substantially similar to, the model and sample forms do not preclude creditors, assignees, and servicers from modifying the disclosures to accommodate particular consumer circumstances or transactions not addressed by the forms. For example, in the case of a consumer bankruptcy or under certain State laws, the creditor, assignee, or servicer may modify the forms to remove language regarding personal liability. A payment-option ARM, which is an ARM permitting consumers to choose among several different payment options for each billing period, is an example of a loan that may require modification of the §1026.20(d) model and sample forms. See appendix H-30(C) for an example of an allocation table for a payment-option loan.*

Section 5: Escrow Account Cancellation
12 C.F.R. § 1026.20(e)

Escrow Account Cancellation - 12 C.F.R § 1026.20(e)

Regulatory Discussion

This section begins with the scope of the requirements in connection with cancelling an escrow account. This section is limited to closed-end consumer transactions secured by a first lien on real property or dwelling, other than a reverse mortgage.

Second, the content requirements include two items.

Third, there is some optional information which the creditor may provide.

Fourth, the format of the disclosure must also meet specific requirements.

Fifth, and finally, there are three timing requirements.

[Logo] [Name of Creditor or Servicer]

Escrow Closing Notice

BORROWER
MAILING ADDRESS

PROPERTY ADDRESS

ISSUE DATE
LENDER
ACCOUNT #/LOAN #

PHONE

As of ____[date]____, you will no longer have an escrow account (also called an "impound" or "trust" account) because

☐ you asked us to close it.

☐ we are closing it.

After this date, you must directly pay your property costs, such as taxes and homeowner's insurance, possibly in one or two large payments a year.

Cost to You	
Escrow Closing Fee *For closing your escrow account*	[dollar amount]

In the future,

If you fail to pay your property taxes, your state or local government may (1) impose fines and penalties or (2) place a tax lien on this property.

If you fail to pay any of your property costs, we may (1) add the amounts to your loan balance, (2) add an escrow account to your loan, or (3) require you to pay for property insurance that we buy on your behalf, which likely would cost more and provide fewer benefits than what you could buy on your own.

Call ____[phone number]____ with any questions about the closing of your escrow account.

☐ We do not offer you the option of keeping the escrow account on your loan.

☐ Contact us at ____[phone number]____ by ____[date]____ if you want to keep the escrow account on your loan.

Regulatory Text

(e) **Escrow account cancellation notice for certain mortgage transactions**

(1) **Scope.** In a closed-end consumer credit transaction secured by a first lien on real property or a dwelling, other than a reverse mortgage subject to §1026.33, for which an escrow account was established in connection with the transaction and will be cancelled, the creditor or servicer shall disclose the information specified in paragraph (e)(2) of this section in accordance with the form requirements in paragraph (e)(4) of this section, and the timing requirements in paragraph (e)(5) of this section. For purposes of this paragraph (e), the term "escrow account" has the same meaning as under 12 CFR 1024.17(b), and the term "servicer" has the same meaning as under 12 CFR 1024.2(b).

(2) **Content requirements.** If an escrow account was established in connection with a transaction subject to this paragraph (e) and the escrow account will be cancelled, the creditor or servicer shall clearly and conspicuously disclose, under the heading "Escrow Closing Notice," the following information:

(i) A statement informing the consumer of the date on which the consumer will no longer have an escrow account; a statement that an escrow account may also be called an impound or trust account; a statement of the reason why the escrow account will be closed; a statement that without an escrow account, the consumer must pay all property costs, such as taxes and homeowner's insurance, directly, possibly in one or two large payments a year; and a table, titled "Cost to you," that contains an itemization of the amount of any fee the creditor or servicer imposes on the consumer in connection with the closure of the consumer's escrow account, labeled "Escrow Closing Fee," and a statement that the fee is for closing the escrow account.

(ii) Under the reference "In the future":

(A) A statement of the consequences if the consumer fails to pay property costs, including the actions that a State or local government may take if property taxes are not paid and the actions the creditor or servicer may take if the consumer does not pay some or all property costs, such as adding amounts to the loan balance, adding an escrow account to the loan, or purchasing a property insurance policy on the consumer's behalf that may be more expensive and provide fewer benefits than a policy that the consumer could obtain directly;

(B) A statement with a telephone number that the consumer can use to request additional information about the cancellation of the escrow account;

(C) A statement of whether the creditor or servicer offers the option of keeping the escrow account open and, as applicable, a telephone number the consumer can use to request that the account be kept open; and

(D) A statement of whether there is a cut-off date by which the consumer can request that the account be kept open.

(3) **Optional information.** The creditor or servicer may, at its option, include its name or logo, the consumer's name, phone number, mailing address and property address,

the issue date of the notice, the loan number, or the consumer's account number on the notice required by this paragraph (e). Except for the name and logo of the creditor or servicer, the information described in this paragraph may be placed between the heading required by paragraph (e)(2) of this section and the disclosures required by paragraphs (e)(2)(i) and (ii) of this section. The name and logo may be placed above the heading required by paragraph (e)(2) of this section.

(4) **Form of disclosures.** The disclosures required by paragraph (e)(2) of this section shall be provided in a minimum 10-point font, grouped together on the front side of a one-page document, separate from all other materials, with the headings, content, order, and format substantially similar to model form H-29 in appendix H to this part. The disclosure of the heading required by paragraph (e)(2) of this section shall be more conspicuous than, and shall precede, the other disclosures required by paragraph (e)(2) of this section.

(5) **Timing**

(i) **Cancellation upon consumer's request.** If the creditor or servicer cancels the escrow account at the consumer's request, the creditor or servicer shall ensure that the consumer receives the disclosures required by paragraph (e)(2) of this section no later than three business days before the closure of the consumer's escrow account.

(ii) **Cancellations other than upon the consumer's request.** If the creditor or servicer cancels the escrow account and the cancellation is not at the consumer's request, the creditor or servicer shall ensure that the consumer receives the disclosures required by paragraph (e)(2) of this section no later than 30 business days before the closure of the consumer's escrow account.

(iii) **Receipt of disclosure**. If the disclosures required by paragraph (e)(2) of this section are not provided to the consumer in person, the consumer is considered to have received the disclosures three business days after they are delivered or placed in the mail.

Regulatory Commentary

20(e) Escrow account cancellation notice for certain mortgage transactions.

20(e)(1) Scope.

*1. **Real property or dwelling.** For purposes of §1026.20(e)(1), the term "real property" includes vacant and unimproved land. The term "dwelling" includes vacation and second homes and mobile homes, boats, and trailers used as residences. See §1026.2(a)(19) and related commentary for additional guidance regarding the term "dwelling."*

*2. **Escrow account established in connection with the consumer's delinquency or default.** Neither creditors nor servicers are required to provide the disclosures required by §1026.20(e)(2) when an escrow account that was established solely in connection with the consumer's delinquency or default on the underlying debt obligation will be cancelled.*

3. ***Termination of the underlying debt obligation.*** *Neither creditors nor servicers are required to provide disclosures required by §1026.20(e)(2) when the underlying debt obligation for which an escrow account was established is terminated, including by repayment, refinancing, rescission, and foreclosure.*

20(e)(2) Content requirements.

1. ***Clear and conspicuous standard.*** *The clear and conspicuous standard generally requires that disclosures be in a reasonably understandable form and readily noticeable to the consumer.*

Paragraph 20(e)(2)(i).

1. ***Escrow closing fee.*** *Section 1026.20(e)(2)(i) requires the creditor to itemize the amount of any fee the creditor or servicer imposes on the consumer in connection with the closure of the consumer's escrow account, labeled "Escrow Closing Fee." If the creditor or servicer independently decides to cancel the escrow account, rather than agreeing to close it at the request of the consumer, and does not charge a fee in connection with the cancellation, the creditor or service complies with §1026.20(e)(2) by leaving the disclosure blank on the front-side of the one-page document described in §1026.20(e)(4).*

20(e)(3) Optional information.

1. ***Optional information permitted.*** *Section 1026.20(e)(3) lists information that the creditor or servicer may, at its option, include on the notice required by §1026.20(e). To comply with §1026.20(e)(3), the creditor or servicer may place the information required by §1026.20(e)(3), other than the name and logo of the creditor or servicer, between the heading required by §1026.20(e)(2) and the disclosures required by §1026.20(e)(2)(i) and (ii). The name and logo may be placed above the heading required §1026.20(e)(2).*

20(e)(4) Form of disclosures.

1. ***Grouped and separate.*** *The disclosures required by §1026.20(e)(2) must be grouped together on the front side of a separate one-page document that contains no other material.*

2. ***Notice must be in writing in a form that the consumer may keep.*** *The notice containing the disclosures required by §1026.20(e)(2) must be in writing in a form that the consumer may keep. See also §1026.17(a) and related commentary for additional guidance on the form requirements applicable to the disclosures required by §1026.20(e)(2).*

20(e)(5) Timing.

20(e)(5)(i) Cancellation upon consumer's request.

1. ***Timing requirements.*** *Section 1026.20(e)(5)(i) provides that if the creditor or servicer cancels the escrow account at the consumer's request, the creditor or servicer shall ensure*

that the consumer receives the disclosures required by §1026.20(e)(2) no later than three business days before closure of the consumer's escrow account. For example, for closure to occur on Thursday, the consumer must receive the disclosures on or before Monday, assuming each weekday is a business day. For purposes of §1026.20(e)(5), the term "business day" means all calendar days except Sundays and legal public holidays referred to in §1026.2(a)(6). See comment 2(a)(6)-2.

20(e)(5)(iii) Receipt of disclosure.

*1. **Timing of receipt.** Section 1026.20(e)(5)(iii) provides that if the disclosures required under §1026.20(e)(2) are not provided to the consumer in person, the consumer is considered to have received the disclosures three business days after they are delivered or placed in the mail. If the creditor or servicer provides the disclosures required by §1026.20(e)(2) by mail, the consumer is considered to have received them three business days after they are placed in the mail for purposes of determining when the waiting periods required by §1026.20(e)(5)(i) and (ii) begins. Creditors and servicers that use electronic mail or a courier to provide disclosures may also follow this approach. If, however, the creditor or servicer delivers the disclosures required by §1026.20(e)(2) to the consumer in person, the escrow account may be closed any time on the third or 30th business day following the date of delivery, as applicable. Whatever method is used to provide disclosures, creditors and servicers may rely on documentation of receipt in determining when the waiting periods required by §1026.20(e)(5)(i) and (ii) begin.*

Right of Rescission – Closed-End Credit

Section 1: Introduction (Commentary)

Regulatory Discussion

This introductory commentary qualifies transactions that are not subject to right-of-rescission.

Regulatory Text

None

Regulatory Commentary

*1. **Transactions not covered.** Credit extensions that are not subject to the regulation are not covered by §1026.23 even if a customer's principal dwelling is the collateral securing the credit. For example, the right of rescission does not apply to a business purpose loan, even though the loan is secured by the customer's principal dwelling.*

Section 2: Consumer's Right to Rescind
12 C.F.R. §1026.23(a)

Consumer's Right to Rescind - 12 CFR § 1026.23(a)

Regulatory Discussion

This section answers the questions:

1. **What transactions are subject to rescission?**
   - a credit transaction in which a security interest is or will be retained or acquired in a consumer's *principal dwelling* (see commentary for additional details).
   - Note: there are exemptions that will be discussed in section 7.
2. **Who has the right to rescind?**
   - Each consumer whose ownership interest is or will be subject to the security interest shall have the right to rescind the transaction, except for transactions described in paragraph (f) of this section.
   - When more than one consumer in a transaction has the right to rescind, the exercise of the right by one consumer shall be effective as to all consumers.
3. **How to rescind?**
   - The consumer shall notify the creditor of the rescission by mail, telegram or other means of written communication (see commentary for additional details).
4. **When to rescind?**
   - The consumer may exercise the right to rescind until midnight of the third *business day* following consummation, delivery of the notice required by paragraph (b) of this section, or delivery of all material disclosures, whichever occurs last.
   - *Business day*, for purposes of rescission, *means all calendar days except Sundays and the legal public holidays* (New Year's Day, the Birthday of Martin Luther King, Jr., Washington's Birthday, Memorial Day, Independence Day, Labor Day, Columbus Day, Veterans Day, Thanksgiving Day, and Christmas Day). See commentary for examples of counting business days.
   - **Exception**: see commentary on *unexpired right of rescission.*

Regulatory Text

(a) **Consumer's right to rescind.**

(1) In a credit transaction in which a security interest is or will be retained or acquired in a consumer's principal dwelling, each consumer whose ownership interest is or will be subject to the security interest shall have the right to rescind the transaction, except for transactions described in paragraph (f) of this section. For purposes of this section, the addition to an existing obligation of a security interest in a consumer's principal dwelling is a transaction. The right of rescission applies only to the addition of the security interest and not the existing obligation. The creditor shall deliver the notice required by paragraph (b) of this section but need not deliver new material disclosures. Delivery of the required

notice shall begin the rescission period.

(2) To exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram or other means of written communication. Notice is considered given when mailed, when filed for telegraphic transmission or, if sent by other means, when delivered to the creditor's designated place of business.

(3)

(i) The consumer may exercise the right to rescind until midnight of the third business day following consummation, delivery of the notice required by paragraph (b) of this section, or delivery of all material disclosures, whichever occurs last. If the required notice or material disclosures are not delivered, the right to rescind shall expire 3 years after consummation, upon transfer of all of the consumer's interest in the property, or upon sale of the property, whichever occurs first. In the case of certain administrative proceedings, the rescission period shall be extended in accordance with section 125(f) of the Act.

(ii) For purposes of this paragraph (a)(3), the term "material disclosures" means the required disclosures of the annual percentage rate, the finance charge, the amount financed, the total of payments, the payment schedule, and the disclosures and limitations referred to in §§1026.32(c) and (d) and 1026.43(g).

(4) When more than one consumer in a transaction has the right to rescind, the exercise of the right by one consumer shall be effective as to all consumers.

Regulatory Commentary

23(a) Consumer's Right to Rescind

Paragraph 23(a)(1)

1. Security interest arising from transaction.

i. In order for the right of rescission to apply, the security interest must be retained as part of the credit transaction. For example:

A. A security interest that is acquired by a contractor who is also extending the credit in the transaction.

B. A mechanic's or materialman's lien that is retained by a subcontractor or supplier of the contractor-creditor, even when the latter has waived its own security interest in the consumer's home.

ii. The security interest is not part of the credit transaction and therefore the transaction is not subject to the right of rescission when, for example:

A. A mechanic's or materialman's lien is obtained by a contractor who is not a party to the credit transaction but is merely paid with the proceeds of the consumer's unsecured bank loan.

B. All security interests that may arise in connection with the credit transaction are validly waived.

C. The creditor obtains a lien and completion bond that in effect satisfies all liens against the consumer's principal dwelling as a result of the credit transaction.

iii. Although liens arising by operation of law are not considered security interests for purposes of disclosure under §1026.2, that section specifically includes them in the definition for purposes of the right of rescission. Thus, even though an interest in the consumer's principal dwelling is not a required disclosure under §1026.18(m), it may still give rise to the right of rescission.

2. ***Consumer.*** *To be a consumer within the meaning of §1026.2, that person must at least have an ownership interest in the dwelling that is encumbered by the creditor's security interest, although that person need not be a signatory to the credit agreement. For example, if only one spouse signs a credit contract, the other spouse is a consumer if the ownership interest of that spouse is subject to the security interest.*

3. ***Principal dwelling.*** *A consumer can only have one principal dwelling at a time. (But see comment 23(a)(1)-4.) A vacation or other second home would not be a principal dwelling. A transaction secured by a second home (such as a vacation home) that is not currently being used as the consumer's principal dwelling is not rescindable, even if the consumer intends to reside there in the future. When a consumer buys or builds a new dwelling that will become the consumer's principal dwelling within one year or upon completion of construction, the new dwelling is considered the principal dwelling if it secures the acquisition or construction loan. In that case, the transaction secured by the new dwelling is a residential mortgage transaction and is not rescindable. For example, if a consumer whose principal dwelling is currently A builds B, to be occupied by the consumer upon completion of construction, a construction loan to finance B and secured by B is a residential mortgage transaction. Dwelling, as defined in §1026.2, includes structures that are classified as personalty under state law. For example, a transaction secured by a mobile home, trailer, or houseboat used as the consumer's principal dwelling may be rescindable.*

4. ***Special rule for principal dwelling.*** *Notwithstanding the general rule that consumers may have only one principal dwelling, when the consumer is acquiring or constructing a new principal dwelling, any loan subject to Regulation Z and secured by the equity in the consumer's current principal dwelling (for example, a bridge loan) is subject to the right of rescission regardless of the purpose of that loan. For example, if a consumer whose principal dwelling is currently A builds B, to be occupied by the consumer upon completion of construction, a construction loan to finance B and secured by A is subject to the right of rescission. A loan secured by both A and B is, likewise, rescindable.*

5. ***Addition of a security interest.*** *Under §1026.23(a), the addition of a security interest in a consumer's principal dwelling to an existing obligation is rescindable even if the existing obligation is not satisfied and replaced by a new obligation, and even if the existing obligation was previously exempt under §1026.3(b). The right of rescission applies only to the added security interest, however, and not to the original obligation. In those situations, only the §1026.23(b) notice need be delivered, not new material disclosures; the rescission period will begin to run from the delivery of the notice.*

Paragraph 23(a)(2)

1. ***Consumer's exercise of right.*** *The consumer must exercise the right of rescission in writing but not necessarily on the notice supplied under §1026.23(b). Whatever the means of sending*

the notification of rescission—mail, telegram or other written means—the time period for the creditor's performance under §1026.23(d)(2) does not begin to run until the notification has been received. The creditor may designate an agent to receive the notification so long as the agent's name and address appear on the notice provided to the consumer under §1026.23(b). Where the creditor fails to provide the consumer with a designated address for sending the notification of rescission, delivering notification to the person or address to which the consumer has been directed to send, payments constitutes delivery to the creditor or assignee. State law determines whether delivery of the notification to a third party other than the person to whom payments are made is delivery to the creditor or assignee, in the case where the creditor fails to designate an address for sending the notification of rescission.

Paragraph 23(a)(3)

1. ***Rescission period.***

- *i. The period within which the consumer may exercise the right to rescind runs for 3 business days from the last of 3 events:*
  - *A. Consummation of the transaction.*
  - *B. Delivery of all material disclosures.*
  - *C. Delivery to the consumer of the required rescission notice.*
- *ii. For example:*
  - *A. If a transaction is consummated on Friday, June 1, and the disclosures and notice of the right to rescind were given on Thursday, May 31, the rescission period will expire at midnight of the third business day after June 1—that is, Tuesday, June 5.*
  - *B. If the disclosures are given and the transaction consummated on Friday, June 1, and the rescission notice is given on Monday, June 4, the rescission period expires at midnight of the third business day after June 4—that is, Thursday, June 7. The consumer must place the rescission notice in the mail, file it for telegraphic transmission, or deliver it to the creditor's place of business within that period in order to exercise the right.*

2. ***Material disclosures.*** *Section 1026.23(a)(3)(ii) sets forth the material disclosures that must be provided before the rescission period can begin to run. Failure to provide information regarding the annual percentage rate also includes failure to inform the consumer of the existence of a variable rate feature. Failure to give the other required disclosures does not prevent the running of the rescission period, although that failure may result in civil liability or administrative sanctions.*

3. ***Unexpired right of rescission.***

- *i. When the creditor has failed to take the action necessary to start the three-business day rescission period running, the right to rescind automatically lapses on the occurrence of the earliest of the following three events:*
  - *A. The expiration of three years after consummation of the transaction.*
  - *B. Transfer of all the consumer's interest in the property.*
  - *C. Sale of the consumer's interest in the property, including a transaction in which the*

consumer sells the dwelling and takes back a purchase money note and mortgage or retains legal title through a device such as an installment sale contract.

ii. Transfer of all the consumers' interest includes such transfers as bequests and gifts. A sale or transfer of the property need not be voluntary to terminate the right to rescind. For example, a foreclosure sale would terminate an unexpired right to rescind. As provided in Section 125 of the Act, the three-year limit may be extended by an administrative proceeding to enforce the provisions of this section. A partial transfer of the consumer's interest, such as a transfer bestowing co-ownership on a spouse, does not terminate the right of rescission.

Paragraph 23(a)(4)

1. ***Joint owners.*** *When more than one consumer has the right to rescind a transaction, any of them may exercise that right and cancel the transaction on behalf of all. For example, if both husband and wife have the right to rescind a transaction, either spouse acting alone may exercise the right and both are bound by the rescission.*

Section 3: Notice of Right to Rescind
12 C.F.R. § 1026.23(b)

Notice of Right to Rescind - 12 CFR § 1026.23(b)

Regulatory Discussion

This section answers the questions:

1. **To whom does the creditor provide the notice?**
   - Each consumer entitled to rescind must be given two copies of the rescission notice and the material disclosures.
   - In a transaction involving joint owners, both of whom are entitled to rescind, both must receive the notice of the right to rescind and disclosures. See the commentary for exaples.
2. **What are the format and content requirements of the notice?**
   - The notice must be on a separate piece of paper, but may appear with other information such as the itemization of the amount financed. The material must be clear and conspicuous, but no minimum type size or other technical requirements are imposed.
   - The notice *must include* five pieces of information (see (b)(1)(i) through (v)).
   - The notice *may include additional information* (see commentary).
3. **When must the creditor give the notice?**
   - The notice need not be given before consummation of the transaction.
   - The creditor may deliver the notice after the transaction is consummated, but the rescission period will not begin to run until the notice is given. See commentary for example.

Regulatory Text

(b)

(1) **Notice of right to rescind.** In a transaction subject to rescission, a creditor shall deliver two copies of the notice of the right to rescind to each consumer entitled to rescind (one copy to each if the notice is delivered in electronic form in accordance with the consumer consent and other applicable provisions of the E-Sign Act). The notice shall be on a separate document that identifies the transaction and shall clearly and conspicuously disclose the following:

(i) The retention or acquisition of a security interest in the consumer's principal dwelling.

(ii) The consumer's right to rescind the transaction.

(iii) How to exercise the right to rescind, with a form for that purpose, designating the address of the creditor's place of business.

(iv) The effects of rescission, as described in paragraph (d) of this section.

(v) The date the rescission period expires.

(2) **Proper form of notice.** To satisfy the disclosure requirements of paragraph (b)(1) of this section, the creditor shall provide the appropriate model form in appendix H of this part or a substantially similar notice.

Regulatory Commentary

23(b)(1) Notice of Right To Rescind

1. ***Who receives notice.*** *Each consumer entitled to rescind must be given two copies of the rescission notice and the material disclosures. In a transaction involving joint owners, both of whom are entitled to rescind, both must receive the notice of the right to rescind and disclosures. For example, if both spouses are entitled to rescind a transaction, each must receive two copies of the rescission notice (one copy to each if the notice is provided in electronic form in accordance with the consumer consent and other applicable provisions of the E-Sign Act) and one copy of the disclosures.*

2. ***Format.*** *The notice must be on a separate piece of paper, but may appear with other information such as the itemization of the amount financed. The material must be clear and conspicuous, but no minimum type size or other technical requirements are imposed. The notices in appendix H provide models that creditors may use in giving the notice.*

3. ***Content.*** *The notice must include all of the information outlined in Section 1026.23(b)(1)(i) through (v). The requirement in §1026.23(b) that the transaction be identified may be met by providing the date of the transaction. The creditor may provide a separate form that the consumer may use to exercise the right of rescission, or that form may be combined with the other rescission disclosures, as illustrated in appendix H. The notice may include additional information related to the required information, such as:*

   i. A description of the property subject to the security interest.

   ii. A statement that joint owners may have the right to rescind and that a rescission by one is effective for all.

   iii. The name and address of an agent of the creditor to receive notice of rescission.

4. ***Time of providing notice.*** *The notice required by §1026.23(b) need not be given before consummation of the transaction. The creditor may deliver the notice after the transaction is consummated, but the rescission period will not begin to run until the notice is given. For example, if the creditor provides the notice on May 15, but disclosures were given and the transaction was consummated on May 10, the 3-business day rescission period will run from May 15.*

Section 4: Delay of Creditor's Performance
12 C.F.R. § 1026.23(c)

Delay of Creditor's Performance - 12 CFR § 1026.23(c)

Regulatory Discussion

The section describes actions the creditor can and cannot take during the rescission period – unless the consumer has waived their right of rescission. The commentary further describes how a creditor can be "reasonably satisfied" the consumer has not rescinded; as well as reminding the creditor to make certain all consumers eligible to rescind have not exercised the right.

Regulatory Text

(c) **Delay of creditor's performance.** Unless a consumer waives the right of rescission under paragraph (e) of this section, no money shall be disbursed other than in escrow, no services shall be performed and no materials delivered until the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded.

Regulatory Commentary

23(c) Delay of Creditor's Performance

*1. **General rule.** Until the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded, the creditor must not, either directly or through a third party:*

i. Disburse loan proceeds to the consumer.

ii. Begin performing services for the consumer.

iii. Deliver materials to the consumer.

*2. **Escrow.** The creditor may disburse loan proceeds during the rescission period in a valid escrow arrangement. The creditor may not, however, appoint the consumer as "trustee" or "escrow agent" and distribute funds to the consumer in that capacity during the delay period.*

*3. **Actions during the delay period.** Section 1026.23(c) does not prevent the creditor from taking other steps during the delay, short of beginning actual performance. Unless otherwise prohibited, such as by state law, the creditor may, for example:*

i. Prepare the loan check.

ii. Perfect the security interest.

iii. Prepare to discount or assign the contract to a third party.

iv. Accrue finance charges during the delay period.

*4. **Delay beyond rescission period.***

i. The creditor must wait until it is reasonably satisfied that the consumer has not rescinded. For example, the creditor may satisfy itself by doing one of the following:

A. Waiting a reasonable time after expiration of the rescission period to allow for delivery of a mailed notice.

B. Obtaining a written statement from the consumer that the right has not been exercised.

ii. When more than one consumer has the right to rescind, the creditor cannot reasonably rely on the assurance of only one consumer, because other consumers may exercise the right.

Section 5: Effects of Rescission
12 C.F.R. § 1026.23(d)

Effects of Rescission - 12 CFR § 1026.23(d)

Regulatory Discussion

This section describes the actions that must be followed in the effect a transaction is rescinded, and include:

1. Termination of security interest
2. Refunds to consumer; Amounts not refundable to consumer; Reflection of security interest termination
3. Property exchange; Reasonable value
4. Modifications

Regulatory Text

(d) **Effects of rescission.**

(1) When a consumer rescinds a transaction, the security interest giving rise to the right of rescission becomes void and the consumer shall not be liable for any amount, including any finance charge.

(2) Within 20 calendar days after receipt of a notice of rescission, the creditor shall return any money or property that has been given to anyone in connection with the transaction and shall take any action necessary to reflect the termination of the security interest.

(3) If the creditor has delivered any money or property, the consumer may retain possession until the creditor has met its obligation under paragraph (d)(2) of this section. When the creditor has complied with that paragraph, the consumer shall tender the money or property to the creditor or, where the latter would be impracticable or inequitable, tender its reasonable value. At the consumer's option, tender of property may be made at the location of the property or at the consumer's residence. Tender of money must be made at the creditor's designated place of business. If the creditor does not take possession of the money or property within 20 calendar days after the consumer's tender, the consumer may keep it without further obligation.

(4) The procedures outlined in paragraphs (d)(2) and (3) of this section may be modified by court order.

Regulatory Commentary

23(d) Effects of Rescission

Paragraph 23(d)(1)

1. ***Termination of security interest.*** *Any security interest giving rise to the right of rescission becomes void when the consumer exercises the right of rescission. The security interest is automatically negated regardless of its status and whether or not it was recorded or perfected. Under §1026.23(d)(2), however, the creditor must take any action necessary to reflect the fact that the security interest no longer exists.*

Paragraph 23(d)(2)

1. ***Refunds to consumer.*** *The consumer cannot be required to pay any amount in the form of money or property either to the creditor or to a third party as part of the credit transaction. Any amounts of this nature already paid by the consumer must be refunded. "Any amount" includes finance charges already accrued, as well as other charges, such as broker fees, application and commitment fees, or fees for a title search or appraisal, whether paid to the creditor, paid directly to a third party, or passed on from the creditor to the third party. It is irrelevant that these amounts may not represent profit to the creditor.*

2. ***Amounts not refundable to consumer.*** *Creditors need not return any money given by the consumer to a third party outside of the credit transaction, such as costs incurred for a building permit or for a zoning variance. Similarly, the term any amount does not apply to any money or property given by the creditor to the consumer; those amounts must be tendered by the consumer to the creditor under §1026.23(d)(3).*

3. ***Reflection of security interest termination.*** *The creditor must take whatever steps are necessary to indicate that the security interest is terminated. Those steps include the cancellation of documents creating the security interest, and the filing of release or termination statements in the public record. In a transaction involving subcontractors or suppliers that also hold security interests related to the credit transaction, the creditor must insure that the termination of their security interests is also reflected. The 20-day period for the creditor's action refers to the time within which the creditor must begin the process. It does not require all necessary steps to have been completed within that time, but the creditor is responsible for seeing the process through to completion.*

Paragraph 23(d)(3)

1. ***Property exchange.*** *Once the creditor has fulfilled its obligations under §1026.23(d)(2), the consumer must tender to the creditor any property or money the creditor has already delivered to the consumer. At the consumer's option, property may be tendered at the location of the property. For example, if lumber or fixtures have been delivered to the consumer's home, the consumer may tender them to the creditor by making them available for pick-up at the home, rather than physically returning them to the creditor's premises. Money already given to the consumer must be tendered at the creditor's place of business.*

2. ***Reasonable value.*** *If returning the property would be extremely burdensome to the consumer, the consumer may offer the creditor its reasonable value rather than returning the property itself. For example, if building materials have already been incorporated into the consumer's dwelling, the consumer may pay their reasonable value.*

Paragraph 23(d)(4)

1. ***Modifications.*** *The procedures outlined in §1026.23(d)(2) and (3) may be modified by a court. For example, when a consumer is in bankruptcy proceedings and prohibited from returning anything to the creditor, or when the equities dictate, a modification might be made. The sequence of procedures under §1026.23(d)(2) and (3), or a court's modification of those procedures under §1026.23(d)(4), does not affect a consumer's substantive right to rescind and to have the loan amount adjusted accordingly. Where the consumer's right to rescind is contested by the creditor, a court would normally determine whether the consumer has a right to rescind and determine the amounts owed before establishing the procedures for the parties to tender any money or property.*

Section 6: Consumer's Waiver of Right to Rescind
12 C.F.R. § 1026.23(e)

Consumer's Waiver of Right to Rescind - 12 CFR § 1026.23(e)

Regulatory Discussion

Caution: waivers of the right to rescind should not be a frequent occurrence.

In the event of a bona fide personal financial emergency, specific procedures must be followed.

Regulatory Text

(e) **Consumer's waiver of right to rescind.** The consumer may modify or waive the right to rescind if the consumer determines that the extension of credit is needed to meet a bona fide personal financial emergency. To modify or waive the right, the consumer shall give the creditor a dated written statement that describes the emergency, specifically modifies or waives the right to rescind, and bears the signature of all the consumers entitled to rescind. Printed forms for this purpose are prohibited.

Regulatory Commentary

23(e) Consumer's Waiver of Right to Rescind

1. ***Need for waiver.*** *To waive the right to rescind, the consumer must have a bona fide personal financial emergency that must be met before the end of the rescission period. The existence of the consumer's waiver will not, of itself, automatically insulate the creditor from liability for failing to provide the right of rescission.*

2. ***Procedure.*** *To waive or modify the right to rescind, the consumer must give a written statement that specifically waives or modifies the right, and also includes a brief description of the emergency. Each consumer entitled to rescind must sign the waiver statement. In a transaction involving multiple consumers, such as a husband and wife using their home as collateral, the waiver must bear the signatures of both spouses.*

Section 7: Exempt Transactions
12 C.F.R. § 1026.23(f)

Exempt Transactions - 12 CFR § 1026.23(f)

Regulatory Discussion

There are five types of transactions that are exempt from the rescission requirements; the most common are ***residential mortgage transactions*** and some ***refinancings.*** Both of these transactions have specific meanings that must be applied (see the commentary for further detail).

Regulatory Text

(f) **Exempt transactions.** The right to rescind does not apply to the following:

(1) A residential mortgage transaction.

(2) A refinancing or consolidation by the same creditor of an extension of credit already secured by the consumer's principal dwelling. The right of rescission shall apply, however, to the extent the new amount financed exceeds the unpaid principal balance, any earned unpaid finance charge on the existing debt, and amounts attributed solely to the costs of the refinancing or consolidation.

(3) A transaction in which a state agency is a creditor.

(4) An advance, other than an initial advance, in a series of advances or in a series of single-payment obligations that is treated as a single transaction under §1026.17(c)(6), if the notice required by paragraph (b) of this section and all material disclosures have been given to the consumer.

(5) A renewal of optional insurance premiums that is not considered a refinancing under §1026.20(a)(5).

Regulatory Commentary

23(f) Exempt Transactions

1. ***Residential mortgage transaction.*** *Any transaction to construct or acquire a principal dwelling, whether considered real or personal property, is exempt. (See the commentary to §1026.23(a).) For example, a credit transaction to acquire a mobile home or houseboat to be used as the consumer's principal dwelling would not be rescindable.*

2. ***Lien status.*** *The lien status of the mortgage is irrelevant for purposes of the exemption in §1026.23(f)(1); the fact that a loan has junior lien status does not by itself preclude application of this exemption. For example, a home buyer may assume the existing first mortgage and create a second mortgage to finance the balance of the purchase price. Such a transaction would not be rescindable.*

3. ***Combined-purpose transaction.*** *A loan to acquire a principal dwelling and make improvements to that dwelling is exempt if treated as one transaction. If, on the other hand, the loan for the acquisition of the principal dwelling and the subsequent advances for improvements are treated as more than one transaction, then only the transaction that finances the acquisition of that dwelling is exempt.*

4. ***New advances.*** *The exemption in §1026.23(f)(2) applies only to refinancings (including consolidations) by the original creditor. The original creditor is the creditor to whom the written agreement was initially made payable. In a merger, consolidation or acquisition, the successor institution is considered the original creditor for purposes of the exemption in §1026.23(f)(2). If the refinancing involves a new advance of money, the amount of the new advance is rescindable. In determining whether there is a new advance, a creditor may rely on the amount financed, refinancing costs, and other figures stated in the latest Truth in Lending disclosures provided to the consumer and is not required to use, for example, more precise information that may only become available when the loan is closed. For purposes of the right of rescission, a new advance does not include amounts attributed solely to the costs of the refinancing. These amounts would include §1026.4(c)(7) charges (such as attorney's fees and title examination and insurance fees, if bona fide and reasonable in amount), as well as insurance premiums and other charges that are not finance charges. (Finance charges on the new transaction—points, for example—would not be considered in determining whether there is a new advance of money in a refinancing since finance charges are not part of the amount financed.) To illustrate, if the sum of the outstanding principal balance plus the earned unpaid finance charge is $50,000 and the new amount financed is $51,000, then the refinancing would be exempt if the extra $1,000 is attributed solely to costs financed in connection with the refinancing that are not finance charges. Of course, if new advances of money are made (for example, to pay for home improvements) and the consumer exercises the right of rescission, the consumer must be placed in the same position as he or she was in prior to entering into the new credit transaction. Thus, all amounts of money (which would include all the costs of the refinancing) already paid by the consumer to the creditor or to a third party as part of the refinancing would have to be refunded to the consumer. (See the commentary to §1026.23(d)(2) for a discussion of refunds to consumers.) A model rescission notice applicable to transactions involving new advances appears in appendix H. The general rescission notice (model form H-8) is the appropriate form for use by creditors not considered original creditors in refinancing transactions.*

5. ***State creditors.*** *Cities and other political subdivisions of states acting as creditors are not exempted from this section.*

6. ***Multiple advances.*** *Just as new disclosures need not be made for subsequent advances when treated as one transaction, no new rescission rights arise so long as the appropriate notice and disclosures are given at the outset of the transaction. For example, the creditor extends credit for home improvements secured by the consumer's principal dwelling, with advances made as repairs progress. As permitted by §1026.17(c)(6), the creditor makes a single set of disclosures at the beginning of the construction period, rather than separate disclosures for each advance. The right of rescission does not arise with each advance. However, if the advances are treated as separate transactions, the right of rescission applies to each advance.*

7. ***Spreader clauses.*** *When the creditor holds a mortgage or deed of trust on the consumer's principal dwelling and that mortgage or deed of trust contains a "spreader clause," subsequent loans made are separate transactions and are subject to the right of rescission. Those loans are rescindable unless the creditor effectively waives its security interest under the spreader clause with respect to the subsequent transactions.*

8. ***Converting open-end to closed-end credit.*** *Under certain state laws, consummation of a closed-end credit transaction may occur at the time a consumer enters into the initial open-end credit agreement. As provided in the commentary to §1026.17(b), closed-end credit disclosures may be delayed under these circumstances until the conversion of the open-end account to a closed-end transaction. In accounts secured by the consumer's principal dwelling, no new right of rescission arises at the time of conversion. Rescission rights under §1026.15 are unaffected.*

Section 8: Tolerances for Accuracy
12 C.F.R. § 1026.23(g)

Tolerances for Accuracy - 12 CFR § 1026.23(g)

Regulatory Discussion

This section describes the tolerances for accuracy of the finance charge (and other disclosures affected by the finance charge); either one-half of 1 percent, or one percent.

Regulatory Text

(g) **Tolerances for accuracy**

(1) **One-half of 1 percent tolerance.** Except as provided in paragraphs (g)(2) and (h)(2) of this section:

(i) The finance charge and other disclosures affected by the finance charge (such as the amount financed and the annual percentage rate) shall be considered accurate for purposes of this section if the disclosed finance charge:

(A) Is understated by no more than 1⁄2 of 1 percent of the face amount of the note or $100, whichever is greater; or

(B) Is greater than the amount required to be disclosed.

(ii) The total of payments for each transaction subject to § 1026.19(e) and (f) shall be considered accurate for purposes of this section if the disclosed total of payments:

(A) Is understated by no more than 1⁄2 of 1 percent of the face amount of the note or $100, whichever is greater; or

(B) Is greater than the amount required to be disclosed.

(2) **One percent tolerance.** In a refinancing of a residential mortgage transaction with a new creditor (other than a transaction covered by § 1026.32), if there is no new advance and no consolidation of existing loans:

(i) The finance charge and other disclosures affected by the finance charge (such as the amount financed and the annual percentage rate) shall be considered accurate for purposes of this section if the disclosed finance charge:

(A) Is understated by no more than 1 percent of the face amount of the note or $100, whichever is greater; or

(B) Is greater than the amount required to be disclosed.

(ii) The total of payments for each transaction subject to § 1026.19(e) and (f) shall be considered accurate for purposes of this section if the disclosed total of payments:

(A) Is understated by no more than 1 percent of the face amount of the note or $100, whichever is greater; or

(B) Is greater than the amount required to be disclosed.

Regulatory Commentary

23(g) Tolerances for Accuracy

1. ***Example.*** *See comment 38(o)-1 for examples illustrating the interaction of the finance charge and total of payments accuracy requirements for each transaction subject to § 1026.19(e) and (f).*

23(g)(2) One Percent Tolerance

1. ***New advance.*** *The phrase "new advance" has the same meaning as in comment 23(f)-4.*

Section 9: Special Rules for Foreclosure
12 C.F.R. § 1026.23(h)

Special Rules for Foreclosure - 12 CFR § 1026.23(h)

Regulatory Discussion

In the event of a foreclosure:

1. The consumer may rescind the transaction if a mortgage broker fee was omitted or a properly completed notice of rescission was not provided.
2. The tolerances for accuracy of the finance charge (and other disclosures affected by the finance charge) are more onerous than described in the previous section 8.

Regulatory Text

(h) **Special rules for foreclosures**

(1) **Right to rescind.** After the initiation of foreclosure on the consumer's principal dwelling that secures the credit obligation, the consumer shall have the right to rescind the transaction if:

(i) A mortgage broker fee that should have been included in the finance charge was not included; or

(ii) The creditor did not provide the properly completed appropriate model form in appendix H of this part, or a substantially similar notice of rescission.

(2) **Tolerance for disclosures**. After the initiation of foreclosure on the consumer's principal dwelling that secures the credit obligation:

(i) The finance charge and other disclosures affected by the finance charge (such as the amount financed and the annual percentage rate) shall be considered accurate for purposes of this section if the disclosed finance charge:

(A) Is understated by no more than $35; or

(B) Is greater than the amount required to be disclosed.

(ii) The total of payments for each transaction subject to § 1026.19(e) and (f) shall be considered accurate for purposes of this section if the disclosed total of payments:

(A) Is understated by no more than $35; or

(B) Is greater than the amount required to be disclosed.

Regulatory Commentary

23(h) Special Rules for Foreclosures

1. ***Rescission.*** *Section 1026.23(h) applies only to transactions that are subject to rescission under §1026.23(a)(1).*

Paragraph 23(h)(1)(i)

1. ***Mortgage broker fees.*** *A consumer may rescind a loan in foreclosure if a mortgage broker fee that should have been included in the finance charge was omitted, without regard to the dollar amount involved. If the amount of the mortgage broker fee is included but misstated the rule in §1026.23(h)(2) applies.*

23(h)(2) Tolerance for Disclosures

1. ***General.*** *The tolerance for disclosure of the finance charge is based on the accuracy of the total finance charge rather than its component charges. For transactions subject to § 1026.19(e) and (f), the tolerance for disclosure of the total of payments is based on the accuracy of the total of payments, taken as a whole, rather than its component charges.*
2. ***Example.*** *See comment 38(o)-1 for examples illustrating the interaction of the finance charge and total of payments accuracy requirements for each transaction subject to § 1026.19(e) and (f).*

NEW MONEY TO THE BANK – MAY OR MAY NOT BE NEW MONEY TO THE CUSTOMER

H-8 – RESCISSION MODEL FORM (GENERAL)

NOTICE OF RIGHT TO CANCEL

Your Right to Cancel

You are entering into a transaction that will result in a [mortgage/lien/security interest] [on/in] your home. You have a legal right under federal law to cancel this transaction, without cost, within three business days from whichever of the following events occurs last:

(1) the date of the transaction, which is ________; or

(2) the date you received your Truth in Lending disclosures; or

(3) the date you received this notice of your right to cancel.

If you cancel the transaction, the [mortgage/lien/security interest] is also cancelled. Within 20 calendar days after we receive your notice, we must take the steps necessary to reflect the fact that the [mortgage/lien/security interest] [on/in] your home has been cancelled, and we must return to you any money or property you have given to us or to anyone else in connection with this transaction. You may keep any money or property we have given you until we have done the things mentioned above, but you must then offer to return the money or property. If it is impractical or unfair for you to return the property, you must offer its reasonable value. You may offer to return the property at your home or at the location of the property. Money must be returned to the address below. If we do not take possession of the money or property within 20 calendar days of your offer, you may keep it without further obligation.

How to Cancel

If you decide to cancel this transaction, you may do so by notifying us in writing, at [creditor's name and business address].

You may use any written statement that is signed and dated by you and states your intention to cancel, or you may use this notice by dating and signing below. Keep one copy of this notice because it contains important information about your rights.

If you cancel by mail or telegram, you must send the notice no later than midnight of [date] (or midnight of the third business day following the latest of the three events listed above). If you send or deliver your written notice to cancel some other way, it must be delivered to the above address no later than that time.

I WISH TO CANCEL

____ ____________________

Consumer's Signature Date

SAME LENDER, SAME CUSTOMER, REFINANCE WITH NEW MONEY

H-9 – RESCISSION MODEL FORM (REFINANCING WITH ORIGINAL CREDITOR)

NOTICE OF RIGHT TO CANCEL
Your Right to Cancel
You are entering into a new transaction to increase the amount of credit previously provided to you.

Your home is the security for this new transaction. You have a legal right under federal law to cancel this new transaction, without cost, within three business days from whichever of the following events occurs last:

(1) the date of this new transaction, which is ________; or
(2) the date you received your new Truth in Lending disclosures; or
(3) the date you received this notice of your right to cancel.

If you cancel this new transaction, it will not affect any amount that you presently owe. Your home is the security for that amount. Within 20 calendar days after we receive your notice of cancellation of this new transaction, we must take the steps necessary to reflect the fact that your home does not secure the increase of credit. We must also return any money you have given to us or anyone else in connection with this new transaction.

You may keep any money we have given you in this new transaction until we have done the things mentioned above, but you must then offer to return the money at the address below.

If we do not take possession of the money within 20 calendar days of your offer, you may keep it without further obligation.

How To Cancel
If you decide to cancel this new transaction, you may do so by notifying us in writing, at

____

(Creditor's name and business address)
You may use any written statement that is signed and dated by you and state your intention to cancel, or you may use this notice by dating and signing below. Keep one copy of this notice because it contains important information about your rights.

If you cancel by mail or telegram, you must send the notice no later than midnight of

____

(Date)
(or midnight of the third business day following the latest of the three events listed above).

If you send or deliver your written notice to cancel some other way, it must be delivered to the above address no later than that time.

I WISH TO CANCEL

____ ____________________

Consumer's Signature Date

Open and Closed End Real Estate Loans

Increases in Interest Rate

Section 1: Increases in Interest Rate
12 C.F.R. § 1026.30

Limitation on Rates - 12 CFR § 1026.30

Regulatory Discussion

There are *two types of transactions* to consider. Any consumer credit *secured by a dwelling*, the maximum interest rate that may be imposed during the term of the obligation when:

1. In *closed-end credit,* the APR may increase after consummation
2. In *open-end credit,* the APR may increase during the plan.

The commentary contains substantial discussion including the following topics:

1. Scope of coverage
2. Refinanced obligations
3. Assumptions
4. Modifications of obligations
5. Land trusts
6. Relationship to other sections
7. Consumer credit contract
8. Manner of stating the maximum interest rate
9. Multiple interest rate ceilings
10. Interest rate charged after default
11. Increasing the maximum interest rate - general rule
12. Increasing the maximum interest rate - assumption of an obligation

Regulatory Text

A creditor shall include in any consumer credit contract secured by a dwelling and subject to the Act and this part the maximum interest rate that may be imposed during the term of the obligation when:

(a) In the case of closed-end credit, the annual percentage rate may increase after consummation, or

(b) In the case of open-end credit, the annual percentage rate may increase during the plan.

Regulatory Commentary

Section 1026.30 - Limitation on Rates

1. Scope of coverage.

i. The requirement of this section applies to consumer credit obligations secured by a dwelling *(as dwelling is defined in §1026.2(a)(19)) in which the annual percentage rate may increase after consummation (or during the term of the plan, in the case of open-end credit) as a result of an increase in the interest rate component of the finance charge—whether those increases are tied to an index or formula or are within a creditor's discretion. The section applies to credit sales as well as loans. Examples of credit obligations subject to this section include:*

A. Dwelling-secured credit obligations that require variable-rate disclosures under the regulation because the interest rate may increase during the term of the obligation.

B. Dwelling-secured open-end credit plans entered into before November 7, 1989 (the effective date of the home equity rules) that are not considered variable-rate obligations for purposes of disclosure under the regulation but where the creditor reserves the contractual right to increase the interest rate—periodic rate and corresponding annual percentage rate - during the term of the plan.

ii. In contrast, credit obligations in which there is no contractual right to increase the interest rate during the term of the obligation are not subject to this section. Examples include:

A. "Shared-equity" or "shared-appreciation" mortgage loans that have a fixed rate of interest and a shared-appreciation feature based on the consumer's equity in the mortgaged property. (The appreciation share is payable in a lump sum at a specified time.)

B. Dwelling-secured fixed-rate closed-end balloon-payment mortgage loans and dwelling-secured fixed-rate open-end plans with a stated term that the creditor may renew at maturity. (Contrast with the renewable balloon-payment mortgage instrument described in comment 17(c)(1)-11.)

C. Dwelling-secured fixed-rate closed-end multiple advance transactions in which each advance is disclosed as a separate transaction.

D. "Price level adjusted mortgages" or other indexed mortgages that have a fixed rate of interest but provide for periodic adjustments to payments and the loan balance to reflect changes in an index measuring prices or inflation.

iii. The requirement of this section does not apply to credit obligations entered into prior to December 9, 1987. Consequently, new advances under open-end credit plans existing prior to December 9, 1987, are not subject to this section.

*2. **Refinanced obligations.** On or after December 9, 1987, when a credit obligation is refinanced, as defined in §1026.20(a), the new obligation is subject to this section if it is dwelling-secured and allows for increases in the interest rate.*

*3. **Assumptions.** On or after December 9, 1987, when a credit obligation is assumed, as defined in §1026.20(b), the obligation becomes subject to this section if it is dwelling-secured and allows for increases in the interest rate.*

*4. **Modifications of obligations.** The modification of an obligation, regardless of when the obligation was entered into, is generally not covered by this section. For example, increasing the credit limit on a dwelling-secured, open-end plan with a variable interest rate entered into before the effective date of the rule does not make the obligation subject to this section. If, however, a security interest in a dwelling is added on or after December 9, 1987, to a credit obligation that allows for interest rate increases, the obligation becomes subject to this section.*

Similarly, if a variable interest rate feature is added to a dwelling-secured credit obligation, the obligation becomes subject to this section.

5. ***Land trusts.*** *In some states, a land trust is used in residential real estate transactions. (See discussion in comment 3(a)-8.) If a consumer-purpose loan that allows for interest rate increases is secured by an assignment of a beneficial interest in a land trust that holds title to a consumer's dwelling, that loan is subject to this section.*

6. ***Relationship to other sections.*** *Unless otherwise provided for in the commentary to this section, other provisions of the regulation such as definitions, exemptions, rules and interpretations also apply to this section where appropriate. To illustrate:*

   i. An adjustable interest rate business-purpose loan is not subject to this section even if the loan is secured by a dwelling because such credit extensions are not subject to the regulation. (See generally §1026.3(a).)

   ii. Creditors subject to this section are only those that fall within the definition of a creditor in §1026.2(a)(17).

7. ***Consumer credit contract.*** *Creditors are required to specify a lifetime maximum interest rate in their credit contracts—the instrument that creates personal liability and generally contains the terms and conditions of the agreement (for example, a promissory note or home-equity line of credit agreement). In some states, the signing of a commitment letter may create a binding obligation, for example, constituting consummation as defined in §1026.2(a)(13). The maximum interest rate must be included in the credit contract, but a creditor may include the rate ceiling in the commitment instrument as well.*

8. ***Manner of stating the maximum interest rate.*** *The maximum interest rate must be stated in the credit contract either as a specific amount or in any other manner that would allow the consumer to easily ascertain, at the time of entering into the obligation, what the rate ceiling will be over the term of the obligation.*

   i. For example, the following statements would be sufficiently specific:

      A. The maximum interest rate will not exceed X%.

      B. The interest rate will never be higher than X percentage points above the initial rate of Y%.

      C. The interest rate will not exceed X%, or X percentage points above [a rate to be determined at some future point in time], whichever is less.

      D. The maximum interest rate will not exceed X%, or the state usury ceiling, whichever is less.

   ii. The following statements would not comply with this section:

      A. The interest rate will never be higher than X percentage points over the prevailing market rate.

      B. The interest rate will never be higher than X percentage points above [a rate to be determined at some future point in time].

      C. The interest rate will not exceed the state usury ceiling which is currently X%.

iii. A creditor may state the maximum rate in terms of a maximum annual percentage rate that may be imposed. Under an open-end credit plan, this normally would be the corresponding annual percentage rate. (See generally §1026.6(a)(1)(ii) and (b)(4)(i)(A).)

*9. **Multiple interest rate ceilings.** Creditors are not prohibited from setting multiple interest rate ceilings. For example, on loans with multiple variable-rate features, creditors may establish a maximum interest rate for each feature. To illustrate, in a variable-rate loan that has an option to convert to a fixed rate, a creditor may set one maximum interest rate for the initially imposed index-based variable-rate feature and another for the conversion option. Of course, a creditor may establish one maximum interest rate applicable to all features.*

*10. **Interest rate charged after default.** State law may allow an interest rate after default higher than the contract rate in effect at the time of default; however, the interest rate after default is subject to a maximum interest rate set forth in a credit obligation that is otherwise subject to this section. This rule applies only in situations in which a post-default agreement is still considered part of the original obligation.*

*11. **Increasing the maximum interest rate - general rule.** Generally, a creditor may not increase the maximum interest rate originally set on a credit obligation subject to this section unless the consumer and the creditor enter into a new obligation. Therefore, under an open-end plan, a creditor may not increase the rate ceiling imposed merely because there is an increase in the credit limit. If an open-end plan is closed and another opened, a new rate ceiling may be imposed. Furthermore, where an open-end plan has a fixed maturity and a creditor renews the plan at maturity, or enters into a closed-end credit transaction, a new maximum interest rate may be set at that time. If the open-end plan provides for a repayment phase, the maximum interest rate cannot be increased when the repayment phase begins unless the agreement provided for such an increase. For a closed-end credit transaction, a new maximum interest rate may be set only if the transaction is satisfied and replaced by a new obligation. (The exceptions in §1026.20(a)(1)-(5) which limit what transactions are considered refinancings for purposes of disclosure do not apply with respect to increasing a rate ceiling that has been imposed; if a transaction is satisfied and replaced, the rate ceiling may be increased.)*

*12. **Increasing the maximum interest rate - assumption of an obligation.** If an obligation subject to this section is assumed by a new obligor and the original obligor is released from liability, the maximum interest rate set on the obligation may be increased as part of the assumption agreement. (This rule applies whether or not the transaction constitutes an assumption as defined in §1026.20(b).)*

Special Rules - Certain Home Mortgage Transactions

Section 1: Relation, Form, Timing
12 C.F.R. § 1026.31(a) through 12 C.F.R. § 1026.31(c)

Relation to Other Subparts: [12 C.F.R. §1026.31(a)]

Regulatory Discussion

The requirements and limitations of this section are in addition to and not in lieu of those contained in other parts of Regulation Z.

Regulatory Text

(a) **Relation to other subparts in this part.** The requirements and limitations of this subpart are in addition to and not in lieu of those contained in other subparts of this part.

Regulatory Commentary

None.

Form of Disclosures: [12 C.F.R. §1026.31(b)]

Regulatory Discussion

All disclosures required by this subpart must be clear and conspicuous, in writing, in a form that the consumer may keep.

Regulatory Text

(b) **Form of disclosures.** The creditor shall make the disclosures required by this subpart clearly and conspicuously in writing, in a form that the consumer may keep. The disclosures required by this subpart may be provided to the consumer in electronic form, subject to compliance with the consumer consent and other applicable provisions of the Electronic Signatures in Global and National Commerce Act (E-Sign Act) (15 U.S.C. 7001 *et seq.*).

Regulatory Commentary

None.

Timing of Disclosure: [12 C.F.R. §1026.31(c)]

Regulatory Discussion

Disclosures for high-cost mortgages. These disclosures must be delivered at least three business days before consummation of a mortgage transaction covered by that section.

Change in terms. After giving the early disclosures, if there is a change in any term, new disclosures must be provided.

Telephone disclosures. A creditor may provide new disclosures by telephone if the consumer initiates the change and if the creditor provides new written disclosures at consummation, and the file has written proof of the oral disclosures.

Consumer's waiver of waiting period before consummation. The consumer may, after receiving the early disclosures, modify or waive the three-day waiting period meet a bona fide personal financial emergency. The regulation explains the process for this.

Disclosures for reverse mortgages. The creditor must furnish these disclosures at least three business days before consummation.

Regulatory Text

(c) **Timing of disclosure**

(1) **Disclosures for high-cost mortgages.** The creditor shall furnish the disclosures required by §1026.32 at least three business days prior to consummation or account opening of a high-cost mortgage as defined in §1026.32(a).

(i) **Change in terms.** After complying with this paragraph (c)(1) and prior to consummation or account opening, if the creditor changes any term that makes the disclosures inaccurate, new disclosures shall be provided in accordance with the requirements of this subpart.

(ii) **Telephone disclosures**. A creditor may provide new disclosures required by paragraph (c)(1)(i) of this section by telephone if the consumer initiates the change and if, prior to or at consummation or account opening:

(A) The creditor provides new written disclosures; and

(B) The consumer and creditor sign a statement that the new disclosures were provided by telephone at least three days prior to consummation or account opening, as applicable.

(iii) **Consumer's waiver of waiting period before consummation or account opening.** The consumer may, after receiving the disclosures required by this paragraph (c)(1), modify or waive the three-day waiting period between delivery of those disclosures and consummation or account opening if the consumer determines that the extension of credit is needed to meet a bona fide personal financial emergency. To modify or waive the right, the consumer shall give the creditor a dated written statement that describes the emergency, specifically modifies or waives the waiting period, and bears the signature of all the consumers entitled to the waiting period. Printed forms for this purpose are prohibited, except when creditors are permitted to use printed forms pursuant to §1026.23(e)(2).

(2) **Disclosures for reverse mortgages.** The creditor shall furnish the disclosures required by §1026.33 at least three business days prior to:

(i) Consummation of a closed-end credit transaction; or

(ii) The first transaction under an open-end credit plan.

Regulatory Commentary

31(c) Timing of Disclosure

*1. **Furnishing disclosures.** Disclosures are considered furnished when received by the consumer.*

31(c)(1) Disclosures for high-cost mortgages.

*1. **Pre-consummation or account opening waiting period.** A creditor must furnish §1026.32 disclosures at least three business days prior to consummation for a closed-end, high-cost mortgage and at least three business days prior to account opening for an open-end, high-cost mortgage. Under §1026.32, "business day" has the same meaning as the rescission rule in comment 2(a)(6)-2—all calendar days except Sundays and the Federal legal holidays listed in 5 U.S.C. 6103(a). However, while the disclosure rule under §§1026.15 and 1026.23 extends to midnight of the third business day, the rule under §1026.32 does not. For example, under §1026.32, if disclosures were provided on a Friday, consummation or account opening could occur any time on Tuesday, the third business day following receipt of the disclosures. If the timing of the rescission rule were to be used, consummation or account opening could not occur until after midnight on Tuesday.*

31(c)(1)(i) Change in Terms

*1. **Redisclosure required.** Creditors must provide new disclosures when a change in terms makes disclosures previously provided under §1026.32(c) inaccurate, including disclosures based on and labeled as an estimate. A change in terms may result from a formal written agreement or otherwise.*

*2. **Premiums or other charges financed at consummation or account opening.** If the consumer finances the payment of premiums or other charges as permitted under §1026.34(a)(10), and as a result the monthly payment differs from what was previously disclosed under §1026.32, redisclosure is required and a new three-day waiting period applies.*

31(c)(1)(ii) Telephone disclosures.

*1. **Telephone disclosures.** Disclosures by telephone must be furnished at least three business days prior to consummation or account opening, as applicable, calculated in accordance with the timing rules under §1026.31(c)(1).*

31(c)(1)(iii) Consumer's waiver of waiting period before consummation or account opening.

*1. **Modification or waiver.** A consumer may modify or waive the right to the three-day waiting period only after receiving the disclosures required by §1026.32 and only if the circumstances meet the criteria for establishing a bona fide personal financial emergency under §1026.23(e). Whether these criteria are met is determined by the facts surrounding individual situations. The imminent sale of the consumer's home at foreclosure during the three-day period is one example of a bona fide personal financial emergency. Each consumer entitled to the three-day waiting period must sign the handwritten statement for the waiver to be effective.*

31(c)(2) Disclosures for Reverse Mortgages

*1. **Business days.** For purposes of providing reverse mortgage disclosures, "business day" has the same meaning as in comment 31(c)(1)-1 - all calendar days except Sundays and the Federal legal holidays listed in 5 U.S.C. 6103(a). This means if disclosures are provided on a Friday, consummation could occur any time on Tuesday, the third business day following receipt of the disclosures.*

*2. **Open-end plans.** Disclosures for open-end reverse mortgages must be provided at least three business days before the first transaction under the plan (see §1026.5(b)(1)).*

Section 2: Basis of Disclosures and Use of Estimates
12 C.F.R. § 1026.31(d)

Basis of Disclosures and Use of Estimates: [12 C.F.R. §1026.31(d)]

Regulatory Discussion

Legal obligation. Disclosures must reflect the terms of the legal obligation.

Estimates. If any information is unknown to the creditor, the creditor must make the disclosure based on the best information reasonably available.

Per-diem interest. Any disclosure affected by the per-diem interest is accurate if the disclosure is based on the information known at the time of disclosure.

Regulatory Text

(d) **Basis of disclosures and use of estimates**

(1) **Legal Obligation.** Disclosures shall reflect the terms of the legal obligation between the parties.

(2) **Estimates.** If any information necessary for an accurate disclosure is unknown to the creditor, the creditor shall make the disclosure based on the best information reasonably available at the time the disclosure is provided, and shall state clearly that the disclosure is an estimate.

(3) **Per-diem interest.** For a transaction in which a portion of the interest is determined on a per-diem basis and collected at consummation, any disclosure affected by the per-diem interest shall be considered accurate if the disclosure is based on the information known to the creditor at the time that the disclosure documents are prepared.

Regulatory Commentary

31(d) Basis of Disclosures and Use of Estimates

*1. **Redisclosure.** Section 1026.31(d) allows the use of estimates when information necessary for an accurate disclosure is unknown to the creditor, provided that the disclosure is clearly identified as an estimate. For purposes of Subpart E, the rule in §1026.31(c)(1)(i) requiring new disclosures when the creditor changes terms also applies to disclosures labeled as estimates.*

31(d)(3) Per-Diem Interest

*1. **Per-diem interest**. This paragraph applies to the disclosure of any numerical amount (such as the finance charge, annual percentage rate, or payment amount) that is affected by the amount* *of the per-diem interest charge that will be collected at consummation. If the amount of per-diem interest used in preparing the disclosures for consummation is based on the information known to the creditor at the time the disclosure document is prepared, the disclosures are considered accurate under this rule, and affected disclosures are also considered accurate, even if the disclosures were not labeled as estimates. (See comment 17(c)(2)(ii)-1 generally.)*

Section 3: Multiple Parties and Subsequent Events 12 C.F.R. § 1026.31(e) and 12 C.F.R. § 1026.31(f)

Multiple Creditors; Multiple Consumers: [12 C.F.R. §1026.31(e)]

Regulatory Discussion

If a transaction involves more than one creditor, only one set of disclosures is required to be given, and the creditors decide who gives the disclosures.

If there is more than one consumer, the disclosures may be made to any consumer who is primarily liable, except for rescission when each consumer who has the right to rescind receives a disclosure.

Regulatory Text

(e) **Multiple creditors; multiple consumers.** If a transaction involves more than one creditor, only one set of disclosures shall be given and the creditors shall agree among themselves which creditor must comply with the requirements that this part imposes on any or all of them. If there is more than one consumer, the disclosures may be made to any consumer who is primarily liable on the obligation. If the transaction is rescindable under §1026.15 or §1026.23, however, the disclosures shall be made to each consumer who has the right to rescind.

Regulatory Commentary

None.

Effect of Subsequent Events: [12 C.F.R. §1026.31(f)]

Regulatory Discussion

If a disclosure becomes inaccurate because of an event that occurs after the creditor delivers the required disclosures, the inaccuracy is not a violation of Regulation Z, although new disclosures may be required.

Regulatory Text

(f) **Effect of subsequent events.** If a disclosure becomes inaccurate because of an event that occurs after the creditor delivers the required disclosures, the inaccuracy is not a violation of Regulation Z (12 CFR part 1026), although new disclosures may be required for mortgages covered by §1026.32 under paragraph (c) of this section, §1026.9(c), §1026.19, or §1026.20.

Regulatory Commentary

None.

Section 4: APR Accuracy and Corrections
12 C.F.R. § 1026.31(g) and 12 C.F.R. § 1026.31(h)

Accuracy of Annual Percentage Rate: [12 C.F.R. §1026.31(g)]

Regulatory Discussion

The APR is considered accurate, if it is accurate according to the requirements and within the tolerances under section 1026.22.

Regulatory Text

(g) **Accuracy of annual percentage rate.** For purposes of section 1026.32, the annual percentage rate shall be considered accurate, and may be used in determining whether a transaction is covered by section 1026.32, if it is accurate according to the requirements and within the tolerances under section 1026.22 for closed-end credit transactions or 1026.6(a) for open-end credit plans. The finance charge tolerances for rescission under section 1026.23(g) or (h) shall not apply for this purpose.

Regulatory Commentary

None.

Corrections and Unintentional Violations - 12 C.F.R. §1026.31(h)

Regulatory Discussion

There are time limits regarding errors. Generally errors, restitution, and modifications must occur in the first 30 days. If this does not happen, the creditor must change terms and make restitution in a manner that assures that the loan no longer meets the high-cost definition.

Regulatory Text

(h) **Corrections and unintentional violations.** A creditor or assignee in a high-cost mortgage, as defined in §1026.32(a), who, when acting in good faith, failed to comply with any requirement under section 129 of the Act will not be deemed to have violated such requirement if the creditor or assignee satisfies either of the following sets of conditions:

(1)

(i) Within 30 days of consummation or account opening and prior to the institution of any action, the consumer is notified of or discovers the violation;

(ii) Appropriate restitution is made within a reasonable time; and

(iii) Within a reasonable time, whatever adjustments are necessary are made to the loan or credit plan to either, at the choice of the consumer:

(A) Make the loan or credit plan satisfy the requirements of 15 U.S.C. 1631-1651; or

(B) Change the terms of the loan or credit plan in a manner beneficial to the consumer so that the loan or credit plan will no longer be a high-cost mortgage.

(2)

(i) Within 60 days of the creditor's discovery or receipt of notification of an unintentional violation or bona fide error and prior to the institution of any action, the consumer is notified of the compliance failure;

(ii) Appropriate restitution is made within a reasonable time; and

(iii) Within a reasonable time, whatever adjustments are necessary are made to the loan or credit plan to either, at the choice of the consumer:

(A) Make the loan or credit plan satisfy the requirements of 15 U.S.C. 1631-1651; or

(B) Change the terms of the loan or credit plan in a manner beneficial to the consumer so that the loan or credit plan will no longer be a high-cost mortgage.

Regulatory Commentary

31(h) Corrections and unintentional violations.

*1. **Notice requirements.** Notice of a violation pursuant to §1026.31(h)(1) or (2) should be in writing. The notice should make the consumer aware of the choices available under §1026.31(h)(1)(iii) and (2)(iii). For notice to be adequate, the consumer should have at least 60 days in which to consider the available options and communicate a choice to the creditor or assignee.*

*2. **Reasonable time.** To claim the benefit of §1026.31(h), a creditor or assignee must implement appropriate restitution and the consumer's elected adjustment within a reasonable time after the consumer provides notice of that election to the creditor or assignee. What length of time is reasonable will depend on what changes to a loan or credit plan's documentation, disclosure, or terms are necessary to effectuate the adjustment. In general, implementing appropriate restitution and completing an adjustment within 30 days of the consumer's providing notice of the election can be considered reasonable.*

Requirements for High-Cost (HOEPA) Mortgages

Section 1: Coverage, Exemptions, and APR
12 C.F.R. §1026.32(a)

Coverage - §1026.32(a)(1)

Regulatory Discussion

This section describes the factors to consider in determining whether a loan is a "high-cost mortgage."

In the broadest terms, a high-cost mortgage is any consumer credit transaction (either closed- or open-end) that is secured by the consumer's principal dwelling *and meets one* of the following three conditions:

- The APR exceeds the "average prime offer rate" (APOR); or
- The transaction's total points and fees exceed amounts adjusted annually on January 1; or
- The creditor can charge a prepayment penalty.

Note each one of the three conditions has additional qualifications. The commentary provides additional information to assist in determining if any of the three conditions exist.

Regulatory Text

(a) **Coverage.**

(1) The requirements of this section apply to a *high-cost mortgage,* which is any consumer credit transaction that is secured by the consumer's principal dwelling, other than as provided in paragraph (a)(2) of this section, and in which:

(i) The annual percentage rate applicable to the transaction, as determined in accordance with paragraph (a)(3) of this section, will exceed the average prime offer rate, as defined in §1026.35(a)(2), for a comparable transaction by more than:

(A) 6.5 percentage points for a first-lien transaction, other than as described in paragraph (a)(1)(i)(B) of this section;

(B) 8.5 percentage points for a first-lien transaction if the dwelling is personal property and the loan amount is less than $50,000; or

(C) 8.5 percentage points for a subordinate-lien transaction; or

(ii) The transaction's total points and fees, as defined in paragraphs (b)(1) and (2) of this section, will exceed:

(A) 5 percent of the total loan amount for a transaction with a loan amount of $20,000 or more; the $20,000 figure shall be adjusted annually on January 1 by the annual percentage change in the Consumer Price Index that was reported on the preceding June 1; or

(B) The lesser of 8 percent of the total loan amount or $1,000 for a transaction with a loan amount of less than $20,000; the $1,000 and $20,000 figures shall be adjusted annually on January 1 by the annual percentage change in the Consumer Price Index that was reported on the preceding June 1; or

(iii) Under the terms of the loan contract or open-end credit agreement, the creditor can charge a prepayment penalty, as defined in paragraph (b)(6) of this section, more than 36 months after consummation or account opening, or prepayment penalties that can exceed, in total, more than 2 percent of the amount prepaid.

Regulatory Commentary

Paragraph 32(a)(1)

*1. The term **high-cost mortgage** includes both a closed-end credit transaction and an open-end credit plan secured by the consumer's principal dwelling. For purposes of determining coverage under §1026.32, an open-end consumer credit transaction is the account opening of an open-end credit plan. An advance of funds or a draw on the credit line under an open-end credit plan subsequent to account opening does not constitute an open-end "transaction."*

Paragraph 32(a)(1)(i).

*1. **Average prime offer rate.** High-cost mortgages include closed- and open-end consumer credit transactions secured by the consumer's principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by the specified amount. The term "average prime offer rate" is defined in §1026.35(a)(2).*

*2. **Comparable transaction.** Guidance for determining a comparable transaction is set forth in comments 35(a)(1)-1 and 35(a)(2)-2 and -3, which direct creditors to published tables of average prime offer rates for fixed- and variable-rate closed-end credit transactions. Creditors opening open-end credit plans must compare the annual percentage rate for the plan to the average prime offer rate for the most closely comparable closed-end transaction. To identify the most closely comparable closed-end transaction, the creditor should identify whether the credit plan is fixed- or variable-rate; if the plan is fixed-rate, the term of the plan to maturity; if the plan is variable-rate, the duration of any initial, fixed-rate period; and the date the interest rate for the plan is set. If a fixed-rate plan has no definite plan length, a creditor must use the average prime offer rate for a 30-year fixed-rate loan. If a variable-rate plan has an optional, fixed-rate feature, a creditor must use the rate table for variable-rate transactions. If a variable-rate plan has an initial, fixed-rate period that is not in whole years, a creditor must identify the most closely-comparable transaction by using the number of whole years closest to the actual fixed-rate period. For example, if a variable-rate plan has an initial fixed-rate period of 20 months, a creditor must use the average prime offer rate for a two-year adjustable-rate loan. If a variable-rate plan has no initial fixed-rate period, or if it has an initial fixed-rate period of less than one year, a creditor must use the average prime offer rate for a one-year adjustable-rate loan. Thus, for example, if the initial fixed-rate period is six months, a creditor must use the average prime offer rate for a one-year adjustable-rate loan.*

*3. **Rate set.** Comment 35(a)(1)-2 provides guidance for determining the average prime offer rate in effect on the date that the interest rate for the transaction is set.*

Paragraph 32(a)(1)(i)(B).

*1. **Loan amount less than $50,000.** The creditor must determine whether to apply the APR threshold in §1026.32(a)(1)(i)(B) based on the loan amount, which is the face amount of the note.*

Paragraph 32(a)(1)(ii).

*1. **Annual adjustment of $1,000 amount.** The $1,000 figure in §1026.32(a)(1)(ii)(B) is adjusted annually on January 1 by the annual percentage change in the CPI that was in effect on the preceding June 1. The Bureau will publish adjustments after the June figures become available each year.*

i. through v. - Omitted.

vi. For 2020, $1,099, reflecting a 2 percent increase in the CPI-U from June 2018 to June 2019, rounded to the nearest whole dollar.

*2. **Historical adjustment of $400 amount.** Prior to January 10, 2014, a mortgage loan was covered by §1026.32 if the total points and fees payable by the consumer at or before loan consummation exceeded the greater of $400 or 8 percent of the total loan amount. The $400 figure was adjusted annually on January 1 by the annual percentage change in the CPI that was in effect on the preceding June 1, as follows:*

i. through xviii. - Omitted

xix. For 2014, $632, reflecting a 1.1 percent increase in the CPI-U from June 2012 to June 2013, rounded to the nearest whole dollar. Note: [Official commentary has not been updated beyond this point in time.]

*3. **Applicable threshold.** For purposes of §1026.32(a)(1)(ii), a creditor must determine the applicable points and fees threshold based on the face amount of the note (or, in the case of an open-end credit plan, the credit limit for the plan when the account is opened). However, the creditor must apply the allowable points and fees percentage to the "total loan amount," as defined in §1026.32(b)(4). For closed-end credit transactions, the total loan amount may be different than the face amount of the note. The $20,000 amount in §1026.32(a)(1)(ii)(A) and (B) is adjusted annually on January 1 by the annual percentage change in the CPI that was in effect on the preceding June 1.*

i. through v. - Omitted.

vi. For 2020, $21,980, reflecting a 2 percent increase in the CPI-U from June 2018 to June 2019, rounded to the nearest whole dollar.

Paragraph 32(a)(1)(iii).

*1. **Maximum period and amount.** Section 1026.32(a)(1)(iii) provides that a closed-end credit transaction or an open-end credit plan is a high-cost mortgage if, under the terms of the loan* *contract or open-end credit agreement, a creditor can charge either a prepayment penalty more than 36 months after consummation or account opening, or total prepayment penalties that exceed 2 percent of any amount prepaid. Section 1026.32(a)(1)(iii) applies only for purposes of determining whether a transaction is subject to the high-cost mortgage requirements and restrictions in §1026.32(c) and (d) and §1026.34. However, if a transaction is subject to those requirements and restrictions by operation of any provision of §1026.32(a)(1), including by operation of §1026.32(a)(1)(iii), then the transaction may not include a prepayment penalty. See §1026.32(d)(6). As a result, §1026.32(a)(1)(iii) effectively establishes a maximum period during which a prepayment penalty may be imposed, and a maximum prepayment penalty amount that may be imposed, on a closed-end credit transaction or open-end credit plan (other than such a mortgage as described in §1026.32(a)(2)) secured by a consumer's principal dwelling. Closed-end credit transactions covered by §1026.43 are subject to the additional prepayment penalty restrictions set forth in §1026.43(g).*

2. ***Examples; open-end credit.*** *If the terms of an open-end credit agreement allow for a prepayment penalty that exceeds 2 percent of the initial credit limit for the plan, the agreement will be deemed to be a transaction with a prepayment penalty that exceeds 2 percent of the "amount prepaid" within the meaning of §1026.32(a)(1)(iii). The following examples illustrate how to calculate whether the terms of an open-end credit agreement comply with the maximum prepayment penalty period and amounts described in §1026.32(a)(1)(iii).*

   i. *Assume that the terms of a home-equity line of credit with an initial credit limit of $10,000 require the consumer to pay a $500 flat fee if the consumer terminates the plan less than 36 months after account opening. The $500 fee constitutes a prepayment penalty under §1026.32(b)(6)(ii), and the penalty is greater than 2 percent of the $10,000 initial credit limit, which is $200. Under §1026.32(a)(1)(iii), the plan is a high-cost mortgage subject to the requirements and restrictions set forth in §§1026.32 and 1026.34.*

   ii. *Assume that the terms of a home-equity line of credit with an initial credit limit of $10,000 and a ten-year term require the consumer to pay a $200 flat fee if the consumer terminates the plan prior to its normal expiration. The $200 prepayment penalty does not exceed 2 percent of the initial credit limit, but the terms of the agreement permit the creditor to charge the fee more than 36 months after account opening. Thus, under §1026.32(a)(1)(iii), the plan is a high-cost mortgage subject to the requirements and restrictions set forth in §§1026.32 and 1026.34.*

   iii. *Assume that, under the terms of a home-equity line of credit with an initial credit limit of $150,000, the creditor may charge the consumer any closing costs waived by the creditor if the consumer terminates the plan less than 36 months after account opening. Assume also that the creditor waived closing costs of $1,000. Bona fide third-party charges comprised $800 of the $1,000 in waived closing costs, and origination charges retained by the creditor or its affiliate comprised the remaining $200. Under §1026.32(b)(6)(ii), the $800 in bona fide third-party charges is not a prepayment penalty, while the $200 for the creditor's own originations costs is a prepayment penalty. The total prepayment penalty of $200 is less than 2 percent of the initial $150,000 credit limit, and the penalty does not apply if the consumer terminates the plan more than 36 months after account opening. Thus, the plan is not a high-cost mortgage under §1026.32(a)(1)(iii).*

Exemptions - §1026.32(a)(2)

Regulatory Discussion

There are exceptions to the coverage rules. This section describes the four transactions that do not apply.

The commentary provides additional information; particularly important for construction-permanent loans.

Regulatory Text

(2) **Exemptions.** This section does not apply to the following:

(i) A reverse mortgage transaction subject to §1026.33;

(ii) A transaction to finance the initial construction of a dwelling;

(iii) A transaction originated by a Housing Finance Agency, where the Housing Finance Agency is the creditor for the transaction; or

(iv) A transaction originated pursuant to the United States Department of Agriculture's Rural Development Section 502 Direct Loan Program.

Regulatory Commentary

32(a)(2) Exemptions

Paragraph 32(a)(2)(ii)

1. ***Construction-permanent loans.*** *Section 1026.32 does not apply to a transaction to finance the initial construction of a dwelling. This exemption applies to a construction-only loan as well as to the construction phase of a construction-to-permanent loan. Section 1026.32 may apply, however, to permanent financing that replaces a construction loan, whether the permanent financing is extended by the same or a different creditor. When a construction loan may be permanently financed by the same creditor, §1026.17(c)(6)(ii) permits the creditor to give either one combined disclosure for both the construction financing and the permanent financing, or a separate set of disclosures for each of the two phases as though they were two separate transactions. See also comment 17(c)(6)-2. Section 1026.17(c)(6)(ii) addresses only how a creditor may elect to disclose a construction to permanent transaction. Which disclosure option a creditor elects under §1026.17(c)(6)(ii) does not affect the determination of whether the permanent phase of the transaction is subject to §1026.32. When the creditor discloses the two phases as separate transactions, the annual percentage rate for the permanent phase must be compared to the average prime offer rate for a transaction that is comparable to the permanent financing to determine coverage under §1026.32. Likewise, a single amount of points and fees, also reflecting the appropriate charges from the permanent phase, must be calculated and compared with the total loan amount to determine coverage under §1026.32. When the creditor*

discloses the two phases as a single transaction, a single annual percentage rate, reflecting the appropriate charges from both phases, must be calculated for the transaction in accordance with §1026.32(a)(3) and appendix D to part 1026. This annual percentage rate must be compared to the average prime offer rate for a transaction that is comparable to the permanent financing to determine coverage under §1026.32. Likewise, a single amount of points and fees, also reflecting the appropriate charges from both phases of the transaction, must be calculated and compared with the total loan amount to determine coverage under §1026.32. If the transaction is determined to be a high-cost mortgage, only the permanent phase is subject to the requirements of §§1026.32 and 1026.34.

Paragraph 32(a)(2)(iii).

*1. **Housing Finance Agency.** For purposes of §1026.32(a)(2)(iii), a Housing Finance Agency means a housing finance agency as defined in 24 CFR 266.5.*

Determination of APR - §1026.32(a)(3)

Regulatory Discussion

This section requires a different calculation of the APR *solely to determine coverage under §1026.32(a)(1)(i)*; based on the following three transaction types:

- A transaction in which the APR *will not vary* during the term of the loan
- A transaction in which the interest rate *may vary* during the term of the loan in accordance with an index
- A transaction in which the interest rate *may or will vary* during the term of the loan

The commentary provides additional information.

Regulatory Text

(3) **Determination of annual percentage rate.** For purposes of paragraph (a)(1)(i) of this section, a creditor shall determine the annual percentage rate for a closed- or open-end credit transaction based on the following:

(i) For a transaction in which the annual percentage rate will not vary during the term of the loan or credit plan, the interest rate in effect as of the date the interest rate for the transaction is set;

(ii) For a transaction in which the interest rate may vary during the term of the loan or credit plan in accordance with an index, the interest rate that results from adding the maximum margin permitted at any time during the term of the loan or credit plan to the value of the index rate in effect as of the date the interest rate for the transaction is set, or the introductory interest rate, whichever is greater; and

(iii) For a transaction in which the interest rate may or will vary during the term of the loan or credit plan, other than a transaction described in paragraph (a)(3)(ii) of this section, the maximum interest rate that may be imposed during the term of the loan or credit plan.

Regulatory Commentary

32(a)(3) Determination of annual percentage rate.

1. ***In general.*** *The guidance set forth in the commentary to §1026.17(c)(1) and in §1026.40 addresses calculation of the annual percentage rate disclosures for closed-end credit transactions and open-end credit plans, respectively. Section 1026.32(a)(3) requires a different calculation of the annual percentage rate solely to determine coverage under §1026.32(a)(1)(i).*

2. ***Open-end credit.*** *The annual percentage rate for an open-end credit plan must be determined in accordance with §1026.32(a)(3), regardless of whether there is an advance of funds at account opening. Section 1026.32(a)(3) does not require the calculation of the annual percentage rate for any extensions of credit subsequent to account opening. Any draw on the credit line subsequent to account opening is not treated as a separate transaction for purposes of determining annual percentage rate threshold coverage.*

3. ***Rates that vary; index rate plus maximum margin.***

   i. *Section 1026.32(a)(3)(ii) applies in the case of a closed- or open-end credit transaction when the interest rate for the transaction varies solely in accordance with an index. For purposes of §1026.32(a)(3)(ii), a transaction's interest rate varies in accordance with an index even if the transaction has an initial rate that is not determined by the index used to make later interest rate adjustments provided that, following the first rate adjustment, the interest rate for the transaction varies solely in accordance with an index.*

   ii. *In general, for transactions subject to §1026.32(a)(3)(ii), the annual percentage rate is determined by adding the index rate in effect on the date that the interest rate for the transaction is set to the maximum margin for the transaction, as set forth in the agreement for the loan or plan. In some cases, a transaction subject to §1026.32(a)(3)(ii) may have an initial rate that is a premium rate and is higher than the index rate plus the maximum margin as of the date the interest rate for the transaction is set. In such cases, the annual percentage rate is determined based on the initial "premium" rate.*

   iii. *The following examples illustrate the rule:*

      A. *Assume that the terms of a closed-end, adjustable-rate mortgage loan provide for a fixed, initial interest rate of 2 percent for two years following consummation, after which the interest rate will adjust annually in accordance with an index plus a 2 percent margin. Also assume that the applicable index is 3 percent as of the date the interest rate for the transaction is set, and a lifetime interest rate cap of 15 percent applies to the transaction. Pursuant to §1026.32(a)(3)(ii), for purposes of determining the annual percentage rate for §1026.32(a)(1)(i), the interest rate for the transaction is 5 percent (3 percent index rate plus 2 percent margin).*

      B. *Assume the same transaction terms set forth in paragraph 3.iii.A, except that an initial interest rate of 6 percent applies to the transaction. Pursuant to §1026.32(a)(3)(ii), for purposes of determining the annual percentage rate for §1026.32(a)(1)(i), the interest rate for the transaction is 6 percent.*

      C. *Assume that the terms of an open-end credit agreement with a five-year draw period and a five-year repayment period provide for a fixed, initial interest rate of 2 percent for the* *first year of the repayment period, after which the interest rate will adjust annually pursuant to a publicly-available index outside the creditor's control, in accordance with the limitations applicable to open-end credit plans in §1026.40(f). Also assume that, pursuant to the terms of the open-end credit agreement, a margin of 2 percent applies because the consumer is employed by the creditor, but that the margin will increase to 4 percent if the consumer's employment with the creditor ends. Finally, assume that the applicable index rate is 3.5 percent as of the date the interest rate for the transaction is set, and a lifetime interest rate cap of 15 percent applies to the transaction. Pursuant to §1026.32(a)(3)(ii), for purposes of determining the annual percentage rate for §1026.32(a)(1)(i), the interest rate for the transaction is 7.5 percent (3.5 percent index rate plus 4 percent maximum margin).*

D. Assume the same transaction terms set forth in paragraph 3.iii.C, except that an initial interest rate of 8 percent applies to the transaction. Pursuant to §1026.32(a)(3)(ii), for purposes of determining the annual percentage rate for §1026.32(a)(1)(i), the interest rate for the transaction is 8 percent.

4. ***Rates that vary other than in accordance with an index.*** *Section 1026.32(a)(3)(iii) applies when the interest rate applicable to a closed- or open-end transaction may or will vary, except as described in §1026.32(a)(3)(ii). Section 1026.32(a)(3)(iii) thus applies where multiple fixed rates apply to a transaction, such as in a step-rate mortgage. For example, assume the following interest rates will apply to a transaction: 3 percent for the first six months, 4 percent for the next 10 years, and 5 percent for the remaining loan term. In this example, §1026.32(a)(3)(iii) would be used to determine the interest rate, and 5 percent would be the maximum interest rate applicable to the transaction used to determine the annual percentage rate for purposes of §1026.32(a)(1)(i). Section 1026.32(a)(3)(iii) also applies to any other adjustable-rate loan where the interest rate may vary but according to a formula other than the sum of an index and a margin.*

5. ***Fixed-rate and -term payment options.*** *If an open-end credit plan has only a fixed rate during the draw period, a creditor must use the interest rate applicable to that feature to determine the annual percentage rate, as required by §1026.32(a)(3)(i). However, if an open-end credit plan has a variable rate, but also offers a fixed-rate and -term payment option during the draw period, §1026.32(a)(3) requires a creditor to use the terms applicable to the variable-rate feature for determining the annual percentage rate, as described in §1026.32(a)(3)(ii).*

Points and Fees - 12 C.F.R. §§ 1026.32(b)(1) and 1025.32(b)(2)

Regulatory Discussion

This section contains the lengthy (and somewhat complex) definition of the term Points and Fees associated with high-cost mortgages:

- Points and fees, *in connection with a closed-end transaction*
- Points and fees, *in connection with an open-end transaction*

With respect to *closed-end transactions*, there are six components, as follows:

- All items included in the finance charge under §1026.4(a) and (b), with exceptions (A) through (F)
- All compensation paid directly or indirectly by a consumer or creditor to a loan originator, as defined in §1026.36(a)(1), that can be attributed to that transaction at the time the interest rate is set, with exceptions (A) through (D)
- All items listed in §1026.4(c)(7) (other than amounts held for future payment of taxes), with exceptions (A) through (C)
- Premiums or other charges payable at or before consummation for any credit life, credit disability, credit unemployment, or credit property insurance, or any other life, accident, health, or loss-of-income insurance for which the creditor is a beneficiary, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract
- The maximum prepayment penalty, as defined in paragraph (b)(6)(i) of this section, that may be charged or collected under the terms of the mortgage loan
- The total prepayment penalty, as defined in paragraph (b)(6)(i) or (ii) of this section, as applicable, incurred by the consumer if the consumer refinances the existing mortgage loan, or terminates an existing open-end credit plan in connection with obtaining a new mortgage loan, with the current holder of the existing loan or plan, a servicer acting on behalf of the current holder, or an affiliate of either

With respect to *open-end transactions*, there are eight components, as follows:

- All items included in the finance charge under §1026.4(a) and (b), with exceptions (A) through (F)
- All compensation paid directly or indirectly by a consumer or creditor to a loan originator, as defined in §1026.36(a)(1), that can be attributed to that transaction at the time the interest rate is set, with exceptions (A) through (D)
- All items listed in §1026.4(c)(7) (other than amounts held for future payment of taxes), with exceptions (A) through (C)
- Premiums or other charges payable at or before account opening for any credit life, credit disability, credit unemployment, or credit property insurance, or any other life,

accident, health, or loss-of-income insurance for which the creditor is a beneficiary, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract

- The maximum prepayment penalty, as defined in paragraph (b)(6)(ii) of this section, that may be charged or collected under the terms of the open-end credit plan
- The total prepayment penalty, as defined in paragraph (b)(6)(i) or (ii) of this section, as applicable, incurred by the consumer if the consumer refinances an existing closed-end credit transaction with an open-end credit plan, or terminates an existing open-end credit plan in connection with obtaining a new open-end credit plan, with the current holder of the existing plan, a servicer acting on behalf of the current holder, or an affiliate of either
- Any fees charged for participation in an open-end credit plan, payable at or before account opening, as described in §1026.4(c)(4)
- Any transaction fee, including any minimum fee or per-transaction fee, that will be charged for a draw on the credit line, where the creditor must assume that the consumer will make at least one draw during the term of the plan

The commentary provides expanded discussion on these items.

Regulatory Text

(b) **Definitions.** For purposes of this subpart, the following definitions apply:

(1) In connection with a closed-end credit transaction, **points and fees** means the following fees or charges that are known at or before consummation:

(i) All items included in the finance charge under §1026.4(a) and (b), except that the following items are excluded:

(A) Interest or the time-price differential;

(B) Any premium or other charge imposed in connection with any Federal or State agency program for any guaranty or insurance that protects the creditor against the consumer's default or other credit loss;

(C) For any guaranty or insurance that protects the creditor against the consumer's default or other credit loss and that is not in connection with any Federal or State agency program:

(1) If the premium or other charge is payable after consummation, the entire amount of such premium or other charge; or

(2) If the premium or other charge is payable at or before consummation, the portion of any such premium or other charge that is not in excess of the amount payable under policies in effect at the time of origination under section 203(c)(2)(A) of the National Housing Act (12 U.S.C. 1709(c)(2)(A)), provided that the premium or charge is required to be refundable on a pro rata basis and the refund is automatically issued upon notification of the satisfaction of the underlying mortgage loan;

(D) Any bona fide third-party charge not retained by the creditor, loan originator, or an affiliate of either, unless the charge is required to be included in points and fees under paragraph (b)(1)(i)(C), (iii), or (iv) of this section;

(E) Up to two bona fide discount points paid by the consumer in connection with the transaction, if the interest rate without any discount does not exceed:

(1) The average prime offer rate, as defined in §1026.35(a)(2), by more than one percentage point; or

(2) For purposes of paragraph (a)(1)(ii) of this section, for transactions that are secured by personal property, the average rate for a loan insured under Title I of the National Housing Act (12 U.S.C. 1702 et seq.) by more than one percentage point; and

(F) If no discount points have been excluded under paragraph (b)(1)(i)(E) of this section, then up to one bona fide discount point paid by the consumer in connection with the transaction, if the interest rate without any discount does not exceed:

(1) The average prime offer rate, as defined in §1026.35(a)(2), by more than two percentage points; or

(2) For purposes of paragraph (a)(1)(ii) of this section, for transactions that are secured by personal property, the average rate for a loan insured under Title I of the National Housing Act (12 U.S.C. 1702 et seq.) by more than two percentage points;

(ii) All compensation paid directly or indirectly by a consumer or creditor to a loan originator, as defined in §1026.36(a)(1), that can be attributed to that transaction at the time the interest rate is set unless:

(A) That compensation is paid by a consumer to a mortgage broker, as defined in §1026.36(a)(2), and already has been included in points and fees under paragraph (b)(1)(i) of this section;

(B) That compensation is paid by a mortgage broker, as defined in §1026.36(a)(2), to a loan originator that is an employee of the mortgage broker;

(C) That compensation is paid by a creditor to a loan originator that is an employee of the creditor; or

(D) That compensation is paid by a retailer of manufactured homes to its employee.

(iii) All items listed in §1026.4(c)(7) (other than amounts held for future payment of taxes), unless:

(A) The charge is reasonable;

(B) The creditor receives no direct or indirect compensation in connection with the charge; and

(C) The charge is not paid to an affiliate of the creditor;

(iv) Premiums or other charges payable at or before consummation for any credit life, credit disability, credit unemployment, or credit property insurance, or any other life, accident, health, or loss-of-income insurance for which the creditor is a beneficiary, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract;

(v) The maximum prepayment penalty, as defined in paragraph (b)(6)(i) of this section, that may be charged or collected under the terms of the mortgage loan; and

(vi) The total prepayment penalty, as defined in paragraph (b)(6)(i) or (ii) of this section, as applicable, incurred by the consumer if the consumer refinances the existing mortgage loan, or terminates an existing open-end credit plan in connection with obtaining a new mortgage loan, with the current holder of the existing loan or plan, a servicer acting on behalf of the current holder, or an affiliate of either.

(2) In connection with an open-end credit plan, **points and fees** means the following fees or charges that are known at or before account opening:

(i) All items included in the finance charge under §1026.4(a) and (b), except that the following items are excluded:

(A) Interest or the time-price differential;

(B) Any premium or other charge imposed in connection with any Federal or State agency program for any guaranty or insurance that protects the creditor against the consumer's default or other credit loss;

(C) For any guaranty or insurance that protects the creditor against the consumer's default or other credit loss and that is not in connection with any Federal or State agency program:

(1) If the premium or other charge is payable after account opening, the entire amount of such premium or other charge; or

(2) If the premium or other charge is payable at or before account opening, the portion of any such premium or other charge that is not in excess of the amount payable under policies in effect at the time of account opening under section 203(c)(2)(A) of the National Housing Act (12 U.S.C. 1709(c)(2)(A)), provided that the premium or charge is required to be refundable on a pro rata basis and the refund is automatically issued upon notification of the satisfaction of the underlying mortgage transaction;

(D) Any bona fide third-party charge not retained by the creditor, loan originator, or an affiliate of either, unless the charge is required to be included in points and fees under paragraphs (b)(2)(i)(C), (b)(2)(iii) or (b)(2)(iv) of this section;

(E) Up to two bona fide discount points payable by the consumer in connection with the transaction, provided that the conditions specified in paragraph (b)(1)(i)(E) of this section are met; and

(F) Up to one bona fide discount point payable by the consumer in connection with the transaction, provided that no discount points have been excluded under paragraph (b)(2)(i)(E) of this section and the conditions specified in paragraph (b)(1)(i)(F) of this section are met;

(ii) All compensation paid directly or indirectly by a consumer or creditor to a loan originator, as defined in §1026.36(a)(1), that can be attributed to that transaction at the time the interest rate is set unless:

(A) That compensation is paid by a consumer to a mortgage broker, as defined in §1026.36(a)(2), and already has been included in points and fees under paragraph (b)(2)(i) of this section;

(B) That compensation is paid by a mortgage broker, as defined in §1026.36(a)(2), to a loan originator that is an employee of the mortgage broker;

(C) That compensation is paid by a creditor to a loan originator that is an employee of the creditor; or

(D) That compensation is paid by a retailer of manufactured homes to its employee.

(iii) All items listed in §1026.4(c)(7) (other than amounts held for future payment of taxes) unless:

(A) The charge is reasonable;

(B) The creditor receives no direct or indirect compensation in connection with the charge; and

(C) The charge is not paid to an affiliate of the creditor;

(iv) Premiums or other charges payable at or before account opening for any credit life, credit disability, credit unemployment, or credit property insurance, or any other life, accident, health, or loss-of-income insurance for which the creditor is a beneficiary, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract;

(v) The maximum prepayment penalty, as defined in paragraph (b)(6)(ii) of this section, that may be charged or collected under the terms of the open-end credit plan;

(vi) The total prepayment penalty, as defined in paragraph (b)(6)(i) or (ii) of this section, as applicable, incurred by the consumer if the consumer refinances an existing closed-end credit transaction with an open-end credit plan, or terminates an existing open-end credit plan in connection with obtaining a new open-end credit plan, with the current holder of the existing transaction or plan, a servicer acting on behalf of the current holder, or an affiliate of either;

(vii) Any fees charged for participation in an open-end credit plan, payable at or before account opening, as described in §1026.4(c)(4); and

(viii) Any transaction fee, including any minimum fee or per-transaction fee, that will be charged for a draw on the credit line, where the creditor must assume that the consumer will make at least one draw during the term of the plan.

Regulatory Commentary

Paragraph 32(b)(1).

1. ***Known at or before consummation.*** *Section 1026.32(b)(1) includes in points and fees for closed-end credit transactions those items listed in §1026.32(b)(1)(i) through (vi) that are known at or before consummation. The following examples clarify how to determine whether a charge or fee is known at or before consummation.*

   i. ***General.*** *In general, a charge or fee is "known at or before consummation" if the creditor knows at or before consummation that the charge or fee will be imposed in connection with the transaction, even if the charge or fee is scheduled to be paid after consummation. Thus, for example, if the creditor charges the consumer $400 for an appraisal conducted by an affiliate of the creditor, the $400 is included in points and fees, even if the consumer finances it and repays it over the loan term, because the creditor knows at or before consummation that the charge or fee is imposed in connection with the transaction. By contrast, if a creditor does not know whether a charge or fee will be imposed, it is not included in points and fees. For example, charges or fees that the creditor may impose if the consumer seeks to modify a loan after consummation are not included in points and fees, because the creditor does not know at or before consummation whether the consumer will seek to modify the loan and therefore incur the fees or charges.*

   ii. ***Prepayment penalties.*** *Notwithstanding the guidance in comment 32(b)(1)-1.i, under §1026.32(b)(1)(v) the maximum prepayment penalty that may be charged or collected under the terms of the mortgage loan is included in points and fees because the amount of the maximum prepayment penalty that may be charged or collected is known at or before consummation.*

   iii. ***Certain mortgage and credit insurance premiums.*** *Notwithstanding the guidance in comment 32(b)(1)-1.i, under §1026.32(b)(1)(i)(C)(1) and (iii) premiums and charges for private mortgage insurance and credit insurance that are payable after consummation are not included in points and fees, even if the amounts of such premiums and charges are known at or before consummation.*

2. ***Charges paid by parties other than the consumer.*** *Under §1026.32(b)(1), points and fees may include charges paid by third parties in addition to charges paid by the consumer. Specifically, charges paid by third parties that fall within the definition of points and fees set forth in §1026.32(b)(1)(i) through (vi) are included in points and fees. In calculating points and fees in connection with a transaction, creditors may rely on written statements from the consumer or third party paying for a charge, including the seller, to determine the source and purpose of any third-party payment for a charge.*

   i. ***Examples - included in points and fees.*** *A creditor's origination charge paid by a consumer's employer on the consumer's behalf that is included in the finance charge as defined in §1026.4(a) or (b), must be included in points and fees under §1026.32(b)(1)(i), unless other exclusions under §1026.4 or §1026.32(b)(1)(i)(A) through (F) apply. In addition, consistent with comment 32(b)(1)(i)-1, a third-party payment of an item excluded from the finance charge under a provision of §1026.4, while not included in the total points and fees under §1026.32(b)(1)(i), may be included under §1026.32(b)(1)(ii) through (vi). For example, a payment by a third party of a creditor-imposed fee for an appraisal performed by an employee of the creditor is included in points and fees under §1026.32(b)(1)(iii). See comment 32(b)(1)(i)-1.*

*ii. **Examples - not included in points and fees.** A charge paid by a third party is not included in points and fees under §1026.32(b)(1)(i) if the exclusions to points and fees in §1026.32(b)(1)(i)(A) through (F) apply. For example, certain bona fide third-party charges not retained by the creditor, loan originator, or an affiliate of either are excluded from points and fees under §1026.32(b)(1)(i)(D), regardless of whether those charges are paid by a third party or the consumer.*

*iii. **Seller's points.** Seller's points, as described in §1026.4(c)(5) and commentary, are excluded from the finance charge and thus are not included in points and fees under §1026.32(b)(1)(i). However, charges paid by the seller for items listed in §1026.32(b)(1)(ii) through (vi) are included in points and fees.*

*iv. **Creditor-paid charges.** Charges that are paid by the creditor, other than loan originator compensation paid by the creditor that is required to be included in points and fees under §1026.32(b)(1)(ii), are excluded from points and fees. See §§1026.32(b)(1)(i)(A), 1026.4(a), and comment 4(a)-(2).*

Paragraph 32(b)(1)(i)

*1. **General.** Section 1026.32(b)(1)(i) includes in the total "points and fees" items included in the finance charge under §1026.4(a) and (b). However, certain items that may be included in the finance charge are excluded from points and fees under §1026.32(b)(1)(i)(A) through (F). Items excluded from the finance charge under other provisions of §1026.4 are not included in the total points and fees under §1026.32(b)(1)(i), but may be included in points and fees under §1026.32(b)(1)(ii) through (vi). To illustrate: A fee imposed by the creditor for an appraisal performed by an employee of the creditor meets the definition of "finance charge" under §1026.4(a) as "any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit." However, §1026.4(c)(7) specifies that appraisal fees are not included in the finance charge. A fee imposed by the creditor for an appraisal performed by an employee of the creditor therefore would not be included in the finance charge and would not be counted in points and fees under §1026.32(b)(1)(i). Section 1026.32(b)(1)(iii), however, expressly includes in points and fees items listed in §1026.4(c)(7) (including appraisal fees) if the creditor receives compensation in connection with the charge. A creditor would receive compensation for an appraisal performed by its own employee. Thus, the appraisal fee in this example must be included in the calculation of points and fees.*

Paragraph 32(b)(1)(i)(B)

*1. **Federal and State mortgage insurance premiums and guaranty fees.** Under §1026.32(b)(1)(i)(B), mortgage insurance premiums or guaranty fees in connection with a Federal or State agency program are excluded from points and fees, even though they are included in the finance charge under §1026.4(a) and (b). For example, if a consumer is required to pay a $2,000 mortgage insurance premium for a loan insured by the Federal Housing Administration, the $2,000 must be included in the finance charge but is not counted in points and fees. Similarly, if a consumer pays a 2 percent funding fee for a loan guaranteed by the U.S. Department of Veterans Affairs or through the U.S Department of Agriculture's Rural Development Single Family Housing Guaranteed Loan Program, the fee is included in the finance charge but is not included in points and fees.*

Paragraph 32(b)(1)(i)(C)

1. ***Private mortgage insurance premiums.***

   i. ***Payable after consummation.*** *Under §1026.32(b)(1)(i)(C)(1), private mortgage insurance premiums payable after consummation are excluded from points and fees.*

   ii. ***Payable at or before consummation.***

      A. ***General.*** *Under §1026.32(b)(1)(i)(C)(2), private mortgage insurance premiums payable at or before consummation (i.e., single or up-front premiums) may be excluded from points and fees, even though they are included in the finance charge under §1026.4(a) and (b). However, the portion of the premium that exceeds the amount payable under policies in effect at the time of origination under section 203(c)(2)(A) of the National Housing Act (12 U.S.C. 1709(c)(2)(A)) is included in points and fees. To determine whether any portion of the premium exceeds the amount payable under policies in effect at the time of origination under section 203(c)(2)(A) of the National Housing Act, a creditor references the premium amount that would be payable for the transaction under that Act, as implemented by applicable regulations and other written authorities issued by the Federal Housing Administration (such as Mortgagee Letters), even if the transaction would not qualify to be insured under that Act (including, for example, because the principal amount exceeds the maximum insurable under that Act).*

      B. ***Non-refundable premiums.*** *To qualify for the exclusion from points and fees, private mortgage insurance premiums payable at or before consummation must be required to be refunded on a pro rata basis and the refund must be automatically issued upon notification of the satisfaction of the underlying mortgage loan.*

      C. ***Example.*** *Assume that a $3,000 private mortgage insurance premium charged on a closed-end mortgage loan is payable at or before closing and is required to be refunded on a pro rata basis and that the refund is automatically issued upon notification of the satisfaction of the underlying mortgage loan. Assume also that the maximum premium allowable under the National Housing Act is $2,000. In this case, the creditor could exclude $2,000 from points and fees but would have to include the $1,000 that exceeds the allowable premium under the National Housing Act. However, if the $3,000 private mortgage insurance premium were not required to be refunded on a pro rata basis or if the refund were not automatically issued upon notification of the satisfaction of the underlying mortgage loan, the entire $3,000 premium would be included in points and fees.*

2. ***Method of paying private mortgage insurance premiums.*** *The portion of any private mortgage insurance premiums payable at or before consummation that does not qualify for an exclusion from points and fees under §1026.32(b)(1)(i)(C)(2) must be included in points and fees for purposes of §1026.32(b)(1)(i) whether paid in cash or financed and whether the insurance is optional or required.*

Paragraph 32(b)(1)(i)(D)

1. ***Charges not retained by the creditor, loan originator, or an affiliate of either.*** *In general, a creditor is not required to count in points and fees any bona fide third-party charge not retained by the creditor, loan originator, or an affiliate of either. For example, if bona fide*

charges are imposed by a third-party settlement agent and are not retained by the creditor, loan originator, or an affiliate of either, those charges are not included in points and fees, even if those charges are included in the finance charge under §1026.4(a)(2). The term loan originator has the same meaning as in §1026.36(a)(1).

2. ***Private mortgage insurance.*** *The exclusion for bona fide third-party charges not retained by the creditor, loan originator, or an affiliate of either is limited by §1026.32(b)(1)(i)(C) in the general definition of "points and fees." Section 1026.32(b)(1)(i)(C) requires inclusion in points and fees of premiums or other charges payable at or before consummation for any private guaranty or insurance protecting the creditor against the consumer's default or other credit loss to the extent that the premium or charge exceeds the amount payable under policies in effect at the time of origination under section 203(c)(2)(A) of the National Housing Act (12 U.S.C. 1709(c)(2)(A)). These premiums or charges must also be included if the premiums or charges are not required to be refundable on a pro-rated basis, or the refund is not required to be automatically issued upon notification of the satisfaction of the underlying mortgage loan. Under these circumstances, even if the premiums or other charges are not retained by the creditor, loan originator, or an affiliate of either, they must be included in the points and fees calculation for qualified mortgages. See comments 32(b)(1)(i)(c)-1 and -2 for further discussion of including private mortgage insurance premiums payable at or before consummation in the points and fees calculation.*

3. ***Real estate-related fees.*** *The exclusion for bona fide third-party charges not retained by the creditor, loan originator, or an affiliate of either is limited by §1026.32(b)(1)(iii) in the general definition of points and fees. Section 1026.32(b)(1)(iii) requires inclusion in points and fees of items listed in §1026.4(c)(7) 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. If a charge is required to be included in points and fees under §1026.32(b)(1)(iii), it may not be excluded under §1026.32(b)(1)(i)(D), even if the criteria for exclusion in §1026.32(b)(1)(i)(D) are satisfied.*

4. ***Credit insurance.*** *The exclusion for bona fide third-party charges not retained by the creditor, loan originator, or an affiliate of either is limited by §1026.32(b)(1)(iv) in the general definition of points and fees. Section 1026.32(b)(1)(iv) requires inclusion in points and fees of premiums and other charges for credit insurance and certain other types of insurance. If a charge is required to be included in points and fees under §1026.32(b)(1)(iv), it may not be excluded under §1026.32(b)(1)(i)(D), even if the criteria for exclusion in §1026.32(b)(1)(i)(D) are satisfied.*

Paragraph 32(b)(1)(i)(E).

1. ***Bona fide discount point.*** *The term bona fide discount point is defined in §1026.32(b)(3).*

2. ***Average prime offer rate.*** *The average prime offer rate for purposes of paragraph (b)(1)(i)(E) of this section is the average prime offer rate that applies to a comparable transaction as of the date the discounted interest rate for the transaction is set. For the meaning of "comparable transaction," refer to comment 35(a)(2)-2. The table of average prime offer rates published by the Bureau indicates how to identify the comparable transaction. See comment 35(a)(2)-2.*

3. ***Example.*** *Assume a transaction that is a first-lien, purchase-money home mortgage with a fixed interest rate and a 30-year term. Assume also that the consumer locks in an interest rate of 6 percent on May 1, 2014 that was discounted from a rate of 6.5 percent because the consumer*

paid two discount points. Finally, assume that the average prime offer rate as of May 1, 2014 for home mortgages with a fixed interest rate and a 30-year term is 5.5 percent. The creditor may exclude two bona fide discount points from the points and fees calculation because the rate from which the discounted rate was derived (6.5 percent) exceeded the average prime offer rate for a comparable transaction as of the date the rate on the transaction was set (5.5 percent) by only 1 percentage point.

Paragraph 32(b)(1)(i)(F)

1. ***Bona fide discount point and average prime offer rate.*** *Comments 32(b)(1)(i)(E)-1 and -2 provide guidance concerning the definition of bona fide discount point and average prime offer rate, respectively.*

2. ***Example.*** *Assume a transaction that is a first-lien, purchase-money home mortgage with a fixed interest rate and a 30-year term. Assume also that the consumer locks in an interest rate of 6 percent on May 1, 2014, that was discounted from a rate of 7 percent because the consumer paid four discount points. Finally, assume that the average prime offer rate as of May 1, 2014, for home mortgages with a fixed interest rate and a 30-year term is 5 percent. The creditor may exclude one discount point from the points and fees calculation because the rate from which the discounted rate was derived (7 percent) exceeded the average prime offer rate for a comparable transaction as of the date the rate on the transaction was set (5 percent) by only 2 percentage points.*

Paragraph 32(b)(1)(ii).

1. ***Loan originator compensation - general.*** *Compensation paid by a consumer or creditor to a loan originator, other than an employee of the creditor, is included in the calculation of points and fees for a transaction, provided that such compensation can be attributed to that particular transaction at the time the interest rate is set. Compensation paid to an employee of a creditor is not included in points and fees. Loan originator compensation includes amounts the loan originator retains and is not dependent on the label or name of any fee imposed in connection with the transaction.*

2. ***Loan originator compensation - attributable to a particular transaction.*** *Loan originator compensation is compensation that is paid by a consumer or creditor to a loan originator that can be attributed to that particular transaction. The amount of compensation that can be attributed to a particular transaction is the dollar value of compensation that the loan originator will receive if the transaction is consummated. As explained in comment 32(b)(1)(ii)-3, the amount of compensation that a loan originator will receive is calculated as of the date the interest rate is set and includes compensation that is paid before, at, or after consummation.*

3. ***Loan originator compensation - timing.*** *Compensation paid to a loan originator that can be attributed to a transaction must be included in the points and fees calculation for that loan regardless of whether the compensation is paid before, at, or after consummation. The amount of loan originator compensation that can be attributed to a transaction is determined as of the date the interest rate is set. Thus, loan originator compensation for a transaction includes compensation that can be attributed to that transaction at the time the creditor sets the interest rate for the transaction, even if that compensation is not paid until after consummation.*

4. ***Loan originator compensation - calculating loan originator compensation in connection with other charges or payments included in the finance charge or made to loan originators.***

   i. ***Consumer payments to mortgage brokers.*** *As provided in §1026.32(b)(1)(ii)(A), consumer payments to a mortgage broker already included in the points and fees calculation under §1026.32(b)(1)(i) need not be counted again under §1026.32(b)(1)(ii). For example, assume a consumer pays a mortgage broker a $3,000 fee for a transaction. The $3,000 mortgage broker fee is included in the finance charge under §1026.4(a)(3). Because the $3,000 mortgage broker fee is already included in points and fees under §1026.32(b)(1)(i), it is not counted again under §1026.32(b)(1)(ii).*

   ii. ***Payments by a mortgage broker to its individual loan originator employee.*** *As provided in §1026.32(b)(1)(ii)(B), compensation paid by a mortgage broker to its individual loan originator employee is not included in points and fees under §1026.32(b)(1)(ii). For example, assume a consumer pays a $3,000 fee to a mortgage broker, and the mortgage broker pays a $1,500 commission to its individual loan originator employee for that transaction. The $3,000 mortgage broker fee is included in points and fees, but the $1,500 commission is not included in points and fees because it has already been included in points and fees as part of the $3,000 mortgage broker fee.*

   iii. ***Creditor's origination fees - loan originator not employed by creditor.*** *Compensation paid by a creditor to a loan originator who is not employed by the creditor is included in the calculation of points and fees under §1026.32(b)(1)(ii). Such compensation is included in points and fees in addition to any origination fees or charges paid by the consumer to the creditor that are included in points and fees under §1026.32(b)(1)(i). For example, assume that a consumer pays to the creditor a $3,000 origination fee and that the creditor pays a mortgage broker $1,500 in compensation attributed to the transaction. Assume further that the consumer pays no other charges to the creditor that are included in points and fees under §1026.32(b)(1)(i) and that the mortgage broker receives no other compensation that is included in points and fees under §1026.32(b)(1)(ii). For purposes of calculating points and fees, the $3,000 origination fee is included in points and fees under §1026.32(b)(1)(i) and the $1,500 in loan originator compensation is included in points and fees under §1026.32(b)(1)(ii), equaling $4,500 in total points and fees, provided that no other points and fees are paid or compensation received.*

5. ***Loan originator compensation - calculating loan originator compensation in manufactured home transactions.***

   i. *If a manufactured home retailer qualifies as a loan originator under §1026.36(a)(1), then compensation that is paid by a consumer or creditor to the retailer for loan origination activities and that can be attributed to the transaction at the time the interest rate is set must be included in points and fees. For example, assume a manufactured home retailer takes a residential mortgage loan application and is entitled to receive at consummation a $1,000 commission from the creditor for taking the mortgage loan application. The $1,000 commission is loan originator compensation that must be included in points and fees.*

   ii. *If the creditor has knowledge that the sales price of a manufactured home includes loan originator compensation, then such compensation can be attributed to the transaction at the time the interest rate is set and therefore is included in points and fees under §1026.32(b)(1)(ii). However, the creditor is not required to investigate the sales price of a manufactured home to determine if the sales price includes loan originator compensation.*

iii. As provided in §1026.32(b)(1)(ii)(D), compensation paid by a manufactured home retailer to its employees is not included in points and fees under §1026.32(b)(1)(ii).

Paragraph 32(b)(1)(iii)

*1. **Other charges.** Section 1026.32(b)(1)(iii) defines points and fees to include all items listed in §1026.4(c)(7), other than amounts held for the future payment of taxes, unless certain exclusions apply. An item listed in §1026.4(c)(7) may be excluded from the points and fees calculation if the charge is reasonable; the creditor receives no direct or indirect compensation from the charge; and the charge is not paid to an affiliate of the creditor. For example, a reasonable fee paid by the consumer to an independent, third-party appraiser may be excluded from the points and fees calculation (assuming no compensation is paid to the creditor or its affiliate and no charge is paid to an affiliate). By contrast, a fee paid by the consumer for an appraisal performed by the creditor must be included in the calculation, even though the fee may be excluded from the finance charge if it is bona fide and reasonable in amount.*

Paragraph 32(b)(1)(iv)

*1. **Credit insurance and debt cancellation or suspension coverage.** In determining points and fees for purposes of §1026.32(b)(1), premiums paid at or before consummation for credit insurance or any debt cancellation or suspension agreement or contract are included in points and fees whether they are paid in cash or, if permitted by applicable law, financed and whether the insurance or coverage is optional or required. Such charges are also included whether the amount represents the entire premium or payment for the coverage or an initial payment.*

*2. **Credit property insurance.** Credit property insurance includes insurance against loss of or damage to personal property, such as a houseboat or manufactured home. Credit property insurance covers the creditor's security interest in the property. Credit property insurance does not include homeowners' insurance, which, unlike credit property insurance, typically covers not only the dwelling but its contents and protects the consumer's interest in the property.*

*3. **Life, accident, health, or loss-of-income insurance.** Premiums or other charges for these types of insurance are included in points and fees only if the creditor is a beneficiary. If the consumer or another person designated by the consumer is the sole beneficiary, then the premiums or other charges are not included in points and fees.*

Paragraph 32(b)(2)

1. See comment 32(b)(1)-2 for guidance concerning the inclusion in points and fees of charges paid by parties other than the consumer.

Paragraph 32(b)(2)(i)

*1. **Finance charge.** The points and fees calculation under §1026.32(b)(2) generally does not include items that are included in the finance charge but that are not known until after account opening, such as minimum monthly finance charges or charges based on account activity or inactivity. Transaction fees also generally are not included in the points and fees calculation, except as provided in §1026.32(b)(2)(vi). See comments 32(b)(1)-1 and 32(b)(1)(i)-1 for additional guidance concerning the calculation of points and fees.*

Paragraph 32(b)(2)(i)(B)

1. See comment 32(b)(1)(i)(B)-1 for further guidance concerning the exclusion of mortgage insurance premiums payable in connection with any Federal or State agency program.

Paragraph 32(b)(2)(i)(C)

1. See comment 32(b)(1)(i)(C)-1 and -2 for further guidance concerning the exclusion of mortgage insurance premiums payable for any guaranty or insurance that protects the creditor against the consumer's default or other credit loss and that is not in connection with any Federal or State agency program.

Paragraph 32(b)(2)(i)(D)

1. For purposes of §1026.32(b)(2)(i)(D), the term loan originator means a loan originator as that term is defined in §1026.36(a)(1), without regard to §1026.36(a)(2). See comments 32(b)(1)(i)(D)-1 through -4 for further guidance concerning the exclusion of bona fide third-party charges from points and fees.

Paragraph 32(b)(2)(i)(E)

1. See comments 32(b)(1)(i)(E)-1 through -3 for further guidance concerning the exclusion of up to two bona fide discount points from points and fees.

Paragraph 32(b)(2)(i)(F)

1. See comments 32(b)(1)(i)(F)-1 and -2 for further guidance concerning the exclusion of up to one bona fide discount point from points and fees.

Paragraph 32(b)(2)(ii)

1. For purposes of §1026.32(b)(2)(ii), the term loan originator means a loan originator as that term is defined in §1026.36(a)(1), without regard to §1026.36(a)(2). See the commentary to §1026.32(b)(1)(ii) for additional guidance concerning the inclusion of loan originator compensation in points and fees.

Paragraph 32(b)(2)(iii)

*1. **Other charges.** See comment 32(b)(1)(iii)-1 for further guidance concerning the inclusion of items listed in §1026.4(c)(7) in points and fees.*

Paragraph 32(b)(2)(iv)

*1. **Credit insurance and debt cancellation or suspension coverage.** See comments 32(b)(1)(iv)-1 through -3 for further guidance concerning the inclusion of premiums for credit insurance and debt cancellation or suspension coverage in points and fees.*

Paragraph 32(b)(2)(vii)

1. ***Participation fees.*** *Fees charged for participation in a credit plan must be included in the points and fees calculation for purposes of §1026.32 if payable at or before account opening. These fees include annual fees or other periodic fees that must be paid as a condition of access to the plan itself. See commentary to §1026.4(c)(4) for a description of these fees.*

Paragraph 32(b)(2)(viii).

1. ***Transaction fees to draw down the credit line.*** *Section 1026.32(b)(2)(viii) requires creditors in open-end credit plans to include in points and fees any transaction fee, including any per-transaction fee, that will be charged for a draw on the credit line. Section 1026.32(b)(2)(viii) requires the creditor to assume that the consumer will make at least one draw during the term of the credit plan. Thus, if the terms of the open-end credit plan permit the creditor to charge a $10 transaction fee each time the consumer draws on the credit line, §1026.32(b)(2)(viii) requires the creditor to include one $10 charge in the points and fees calculation.*
2. ***Fixed-rate loan option.*** *If the terms of an open-end credit plan permit a consumer to draw on the credit line using either a variable-rate feature or a fixed-rate feature, §1026.32(b)(2)(viii) requires the creditor to use the terms applicable to the variable-rate feature for determining the transaction fee that must be included in the points and fees calculation.*

Other Definitions – 12 CFR § 1026.32(b)(3) through (b)(6)

Regulatory Discussion

This section defines the remaining terms (relatively straightforward compared to Points and Fees) associated with high-cost mortgages **for both open and closed end credit**:

- Bona fide discount point:
- Total loan amount:
- Affiliate
- Prepayment penalty:

Regulatory Text

(3) **Bona fide discount point**

(i) **Closed-end credit.** The term *bona fide discount point* means an amount equal to 1 percent of the loan amount paid by the consumer that reduces the interest rate or time-price differential applicable to the transaction based on a calculation that is consistent with established industry practices for determining the amount of reduction in the interest rate or time-price differential appropriate for the amount of discount points paid by the consumer.

(ii) **Open-end credit.** The term *bona fide discount point* means an amount equal to 1 percent of the credit limit for the plan when the account is opened, paid by the consumer, and that reduces the interest rate or time-price differential applicable to the transaction based on a calculation that is consistent with established industry practices for determining the amount of reduction in the interest rate or time-price differential appropriate for the amount of discount points paid by the consumer. See comment 32(b)(3)(i)-1 for additional guidance in determining whether a discount point is bona fide.

(4) **Total loan amount**

(i) **Closed-end credit.** The total loan amount for a closed-end credit transaction is calculated by taking the amount financed, as determined according to §1026.18(b), and deducting any cost listed in §1026.32(b)(1)(iii), (iv), or (vi) that is both included as points and fees under §1026.32(b)(1) and financed by the creditor.

(ii) **Open-end credit.** The total loan amount for an open-end credit plan is the credit limit for the plan when the account is opened.

(5) **Affiliate** means any company that controls, is controlled by, or is under common control with another company, as set forth in the Bank Holding Company Act of 1956 (12 U.S.C. 1841 *et seq.*).

(6) **Prepayment penalty**

(i) **Closed-end credit transactions.** For a closed-end credit transaction, *prepayment penalty* means a charge imposed for paying all or part of the transaction's principal before the date on which the principal is due, other than a waived, bona fide third-party charge that the creditor imposes if the consumer prepays all of the transaction's principal sooner than 36 months after consummation, provided, however, that interest charged consistent with the monthly interest accrual amortization method is not a prepayment penalty for extensions of credit insured by the Federal Housing Administration that are consummated before January 21, 2015.

(ii) **Open-end credit.** For an open-end credit plan, *prepayment penalty* means a charge imposed by the creditor if the consumer terminates the open-end credit plan prior to the end of its term, other than a waived, bona fide third-party charge that the creditor imposes if the consumer terminates the open-end credit plan sooner than 36 months after account opening.

Regulatory Commentary

32(b)(3) Bona fide discount point

32(b)(3)(i) Closed-end credit

1. ***Definition of bona fide discount point.*** *Section 1026.32(b)(3) provides that, to be bona fide, a discount point must reduce the interest rate based on a calculation that is consistent with established industry practices for determining the amount of reduction in the interest rate or time-price differential appropriate for the amount of discount points paid by the consumer. To satisfy this standard, a creditor may show that the reduction is reasonably consistent with* *established industry norms and practices for secondary mortgage market transactions. For example, a creditor may rely on pricing in the to-be-announced (TBA) market for mortgage-backed securities (MBS) to establish that the interest rate reduction is consistent with the compensation that the creditor could reasonably expect to receive in the secondary market. The creditor may also establish that its interest rate reduction is consistent with established industry practices by showing that its calculation complies with requirements prescribed in Fannie Mae or Freddie Mac guidelines for interest rate reductions from bona fide discount points. For example, assume that the Fannie Mae Single-Family Selling Guide or the Freddie Mac Single Family Seller/Servicer Guide imposes a cap on points and fees but excludes from the cap discount points that result in a bona fide reduction in the interest rate. Assume the guidelines require that, for a discount point to be bona fide so that it would not count against the cap, a discount point must result in at least a 25 basis point reduction in the interest rate. Accordingly, if the creditor offers a 25 basis point interest rate reduction for a discount point and the requirements of §1026.32(b)(1)(i)(E) or (F) are satisfied, the discount point is bona fide and is excluded from the calculation of points and fees.*

32(b)(4) Total loan amount

32(b)(4)(i) Closed-end credit

1. ***Total loan amount; examples.*** *Below are several examples showing how to calculate the total loan amount for closed-end mortgage loans, each using a $10,000 amount borrowed, a $300 appraisal fee, and $400 in prepaid finance charges. A $500 single premium for optional credit unemployment insurance is used in one example.*

   i. *If the consumer finances a $300 fee for a creditor-conducted appraisal and pays $400 in prepaid finance charges at closing, the amount financed under §1026.18(b) is $9,900 ($10,000 plus the $300 appraisal fee that is paid to and financed by the creditor, less $400 in prepaid finance charges). The $300 appraisal fee paid to the creditor is added to other points and fees under §1026.32(b)(1)(iii). It is deducted from the amount financed ($9,900) to derive a total loan amount of $9,600.*

   ii. *If the consumer pays the $300 fee for the creditor-conducted appraisal in cash at closing, the $300 is included in the points and fees calculation because it is paid to the creditor. However, because the $300 is not financed by the creditor, the fee is not part of the amount financed under §1026.18(b). In this case, the amount financed is the same as the total loan amount: $9,600 ($10,000, less $400 in prepaid finance charges).*

   iii. *If the consumer finances a $300 fee for an appraisal conducted by someone other than the creditor or an affiliate, the $300 fee is not included with other points and fees under §1026.32(b)(1)(iii). In this case, the amount financed is the same as the total loan amount: $9,900 ($10,000 plus the $300 fee for an independently-conducted appraisal that is financed by the creditor, less the $400 paid in cash and deducted as prepaid finance charges).*

   iv. *If the consumer finances a $300 fee for a creditor-conducted appraisal and a $500 single premium for optional credit unemployment insurance, and pays $400 in prepaid finance charges at closing, the amount financed under §1026.18(b) is $10,400 ($10,000, plus the $300 appraisal fee that is paid to and financed by the creditor, plus the $500 insurance premium that is financed by the creditor, less $400 in prepaid finance charges). The $300 appraisal fee paid to the creditor is added to other points and fees under §1026.32(b)(1)(ii),* *and the $500 insurance premium is added under 1026.32(b)(1)(iv). The $300 and $500 costs are deducted from the amount financed ($10,400) to derive a total loan amount of $9,600.*

32(b)(6) Prepayment penalty

1. ***Examples of prepayment penalties; closed-end credit transactions.*** *For purposes of §1026.32(b)(6)(i), the following are examples of prepayment penalties:*

   i. *A charge determined by treating the loan balance as outstanding for a period of time after prepayment in full and applying the interest rate to such "balance," even if the charge results from interest accrual amortization used for other payments in the transaction under the terms of the loan contract. "Interest accrual amortization" refers to the method by which the amount of interest due for each period (e.g., month) in a transaction's term is determined. For example, "monthly interest accrual amortization" treats each payment as made on the scheduled, monthly due date even if it is actually paid early or late (until the expiration of any grace period). Thus, under the terms of a loan contract providing for monthly interest accrual amortization, if the amount of interest due on May 1 for the preceding month of April is $3,000, the loan contract will require payment of $3,000 in interest for the month of April whether the payment is made on April 20, on May 1, or on May 10. In this example, if the consumer prepays the loan in full on April 20 and if the accrued interest as of that date is $2,000, then assessment of a charge of $3,000 constitutes a prepayment penalty of $1,000 because the amount of interest actually earned through April 20 is only $2,000.*

   ii. *A fee, such as an origination or other loan closing cost, that is waived by the creditor on the condition that the consumer does not prepay the loan. However, the term prepayment penalty does not include a waived bona fide third-party charge imposed by the creditor if the consumer pays all of a covered transaction's principal before the date on which the principal is due sooner than 36 months after consummation. For example, assume that at consummation, the creditor waives $3,000 in closing costs to cover bona fide third-party charges but the terms of the loan agreement provide that the creditor may recoup the $3,000 in waived charges if the consumer repays the entire loan balance sooner than 36 months after consummation. The $3,000 charge is not a prepayment penalty. In contrast, for example, assume that at consummation, the creditor waives $3,000 in closing costs to cover bona fide third-party charges but the terms of the loan agreement provide that the creditor may recoup $4,500, in part to recoup waived charges, if the consumer repays the entire loan balance sooner than 36 months after consummation. The $3,000 that the creditor may impose to cover the waived bona fide third-party charges is not a prepayment penalty, but the additional $1,500 charge is a prepayment penalty and subject to the restrictions under §1026.43(g).*

   iii. *A minimum finance charge in a simple interest transaction.*

   iv. *Computing a refund of unearned interest by a method that is less favorable to the consumer than the actuarial method, as defined by section 933(d) of the Housing and Community Development Act of 1992, 15 U.S.C. 1615(d). For purposes of computing a refund of unearned interest, if using the actuarial method defined by applicable State law results in a refund that is greater than the refund calculated by using the method described in section 933(d) of the Housing and Community Development Act of 1992, creditors should use the State law definition in determining if a refund is a prepayment penalty.*

2. ***Fees that are not prepayment penalties; closed-end credit transactions.*** *For purposes of §1026.32(b)(6)(i), fees that are not prepayment penalties include, for example:*

   i. *Fees imposed for preparing and providing documents when a loan is paid in full if such fees are imposed whether or not the loan is prepaid. Examples include a loan payoff statement, a reconveyance document, or another document releasing the creditor's security interest in the dwelling that secures the loan.*

   ii. *Loan guarantee fees.*

3. ***Examples of prepayment penalties; open-end credit.*** *For purposes of §1026.32(b)(6)(ii), the term prepayment penalty includes a charge, including a waived closing cost, imposed by the creditor if the consumer terminates the open-end credit plan prior to the end of its term. This includes a charge imposed if the consumer terminates the plan outright or, for example, if the consumer terminates the plan in connection with obtaining a new loan or plan with the current holder of the existing plan, a servicer acting on behalf of the current holder, or an affiliate of either. However, the term prepayment penalty does not include a waived bona fide third-party charge imposed by the creditor if the consumer terminates the open-end credit plan during the first 36 months after account opening.*

4. ***Fees that are not prepayment penalties; open-end credit.*** *For purposes of §1026.32(b)(6)(ii), fees that are not prepayment penalties include, for example:*

   i. *Fees imposed for preparing and providing documents when an open-end credit plan is terminated, if such fees are imposed whether or not the consumer terminates the plan prior to the end of its term. Examples include a payoff statement, a reconveyance document, or another document releasing the creditor's security interest in the dwelling that secures the line of credit.*

   ii. *Loan guarantee fees.*

   iii. *Any fee that the creditor may impose in lieu of termination and acceleration under comment 40(f)(2)-2.*

Disclosures – 12 CFR § 1026.32(c)(1) through (c)(5)

Regulatory Discussion

Relative to "high-cost mortgage" (HOEPA) transactions, the following additional five disclosures must be made:

1. Notice
2. APR
3. Regular payment; minimum periodic payment example; balloon payment:
   i. Closed-end transactions
   ii. Open-end transactions
4. Variable-rate
5. Amount borrowerd; credit limit:
   i. Closed-end transactions
   ii. Open-end transactions

The commentary provides additional discussion on these items.

Regulatory Text

(c) **Disclosures.** In addition to other disclosures required by this part, in a mortgage subject to this section, the creditor shall disclose the following in conspicuous type size:

(1) **Notices.** The following statement: "You are not required to complete this agreement merely because you have received these disclosures or have signed a loan application. If you obtain this loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the loan."

(2) **Annual percentage rate.** The annual percentage rate.

(3) **Regular payment; minimum periodic payment example; balloon payment.**

(i) For a closed-end credit transaction, the amount of the regular monthly (or other periodic) payment and the amount of any balloon payment provided in the credit contract, if permitted under paragraph (d)(1) of this section. The regular payment disclosed under this paragraph shall be treated as accurate if it is based on an amount borrowed that is deemed accurate and is disclosed under paragraph (c)(5) of this section.

(ii) For an open-end credit plan:

(A) An example showing the first minimum periodic payment for the draw period, the first minimum periodic payment for any repayment period, and the balance outstanding at the beginning of any repayment period. The example must be based on the following assumptions:

(1) The consumer borrows the full credit line, as disclosed in paragraph (c)(5) of this section, at account opening and does not obtain any additional extensions of credit;

(2) The consumer makes only minimum periodic payments during the draw period and any repayment period; and

(3) The annual percentage rate used to calculate the example payments remains the same during the draw period and any repayment period. The creditor must provide the minimum periodic payment example based on the annual percentage rate for the plan, as described in paragraph (c)(2) of this section, except that if an introductory annual percentage rate applies, the creditor must use the rate that will apply to the plan after the introductory rate expires.

(B) If the credit contract provides for a balloon payment under the plan as permitted under paragraph (d)(1) of this section, a disclosure of that fact and an example showing the amount of the balloon payment based on the assumptions described in paragraph (c)(3)(ii)(A) of this section.

(C) A statement that the example payments show the first minimum periodic payments at the current annual percentage rate if the consumer borrows the maximum credit available when the account is opened and does not obtain any additional extensions of credit, or a substantially similar statement.

(D) A statement that the example payments are not the consumer's actual payments and that the actual minimum periodic payments will depend on the amount the consumer borrows, the interest rate applicable to that period, and whether the consumer pays more than the required minimum periodic payment, or a substantially similar statement.

(4) **Variable-rate.** For variable-rate transactions, a statement that the interest rate and monthly payment may increase, and the amount of the single maximum monthly payment, based on the maximum interest rate required to be included in the contract by §1026.30.

(5) **Amount borrowed; credit limit.**

(i) For a closed-end credit transaction, the total amount the consumer will borrow, as reflected by the face amount of the note. Where the amount borrowed includes financed charges that are not prohibited under §1026.34(a)(10), that fact shall be stated, grouped together with the disclosure of the amount borrowed. The disclosure of the amount borrowed shall be treated as accurate if it is not more than $100 above or below the amount required to be disclosed.

(ii) For an open-end credit plan, the credit limit for the plan when the account is opened.

Regulatory Commentary

32(c)(2) Annual percentage rate.

1. ***Disclosing annual percentage rate for open-end high-cost mortgages.*** *In disclosing the annual percentage rate for an open-end, high-cost mortgage under §1026.32(c)(2), creditors* *must comply with §1026.6(a)(1). If a fixed-rate, discounted introductory or initial interest rate is offered on the transaction, §1026.32(c)(2) requires a creditor to disclose the annual percentage rate of the fixed-rate, discounted introductory or initial interest rate feature, and the rate that would apply when the feature expires.*

32(c)(3) Regular payment; minimum periodic payment example; balloon payment.

1. ***Balloon payment.*** *Except as provided in §1026.32(d)(1)(ii) and (iii), a mortgage transaction subject to this section may not include a payment schedule that results in a balloon payment.*

Paragraph 32(c)(3)(i).

1. ***General.*** *The regular payment is the amount due from the consumer at regular intervals, such as monthly, bimonthly, quarterly, or annually. There must be at least two payments, and the payments must be in an amount and at such intervals that they fully amortize the amount owed. In disclosing the regular payment, creditors may rely on the rules set forth in §1026.18(g); however, the amounts for voluntary items, such as credit life insurance, may be included in the regular payment disclosure only if the consumer has previously agreed to the amounts.*

    i. *If the loan has more than one payment level, the regular payment for each level must be disclosed. For example:*

        A. *In a 30-year graduated payment mortgage where there will be payments of $300 for the first 120 months, $400 for the next 120 months, and $500 for the last 120 months, each payment amount must be disclosed, along with the length of time that the payment will be in effect.*

        B. *If interest and principal are paid at different times, the regular amount for each must be disclosed.*

        C. *In discounted or premium variable-rate transactions where the creditor sets the initial interest rate and later rate adjustments are determined by an index or formula, the creditor must disclose both the initial payment based on the discount or premium and the payment that will be in effect thereafter. Additional explanatory material which does not detract from the required disclosures may accompany the disclosed amounts. For example, if a monthly payment is $250 for the first six months and then increases based on an index and margin, the creditor could use language such as the following: "Your regular monthly payment will be $250 for six months. After six months your regular monthly payment will be based on an index and margin, which currently would make your payment $350. Your actual payment at that time may be higher or lower."*

32(c)(4) Variable-rate.

1. ***Calculating "worst-case" payment example.*** *For a closed-end credit transaction, creditors may rely on instructions in §1026.19(b)(2)(viii)(B) for calculating the maximum possible increases in rates in the shortest possible timeframe, based on the face amount of the note (not the hypothetical loan amount of $10,000 required by §1026.19(b)(2)(viii)(B)). The creditor must provide a maximum payment for each payment level, where a payment schedule provides for more than one payment level and more than one maximum payment amount is possible. For an open-end credit plan, the maximum monthly payment must be based on the following assumptions:*

i. The consumer borrows the full credit line at account opening with no additional extensions of credit.

ii. The consumer makes only minimum periodic payments during the draw period and any repayment period.

iii. If the annual percentage rate may increase during the plan, the maximum annual percentage rate that is included in the contract, as required by §1026.30, applies to the plan at account opening.

32(c)(5) Amount Borrowed

1. ***Optional insurance; debt-cancellation coverage.*** *This disclosure is required when the amount borrowed in a refinancing includes premiums or other charges for credit life, accident, health, or loss-of-income insurance, or debt-cancellation coverage (whether or not the debt-cancellation coverage is insurance under applicable law) that provides for cancellation of all or part of the consumer's liability in the event of the loss of life, health, or income or in the case of accident. See comment 4(d)(3)-2 and comment app. G and H-2 regarding terminology for debt-cancellation coverage.*

Section 4: Limitations
12 C.F.R. § 1026.32(d)

Limitations -12 CFR § 1026.32(d)(1) through (d)(8)

Regulatory Discussion

Finally, there are eight limitations with respect to "high-cost mortgages;" as follows:

1. Balloon payments. Note exceptions exist as described in (d)(1)(ii)(A) through (C); as well as for open-end credit plans
2. Negative amortization
3. Advance payments
4. Increased interest rate
5. Rebates
6. Prepayment penalties
7. Reserved
8. Acceleration of debt

The commentary provides additional discussion of these limitations.

Regulatory Text

(d) **Limitations.** A high-cost mortgage shall not include the following terms:

(1)

(i) **Balloon payment.** Except as provided by paragraphs (d)(1)(ii) and (iii) of this section, a payment schedule with a payment that is more than two times a regular periodic payment.

(ii) **Exceptions.** The limitations in paragraph (d)(1)(i) of this section do not apply to:

(A) A mortgage transaction with a payment schedule that is adjusted to the seasonal or irregular income of the consumer;

(B) A loan with maturity of 12 months or less, if the purpose of the loan is a "bridge" loan connected with the acquisition or construction of a dwelling intended to become the consumer's principal dwelling; or

(C) A loan that meets the criteria set forth in §§1026.43(f)(1)(i) through (vi) and 1026.43(f)(2), or the conditions set forth in §1026.43(e)(6).

(iii) **Open-end credit plans.** If the terms of an open-end credit plan provide for a repayment period during which no further draws may be taken, the limitations in paragraph (d)(1)(i) of this section do not apply to any adjustment in the regular periodic payment that results solely from the credit plan's transition from the draw period to the repayment period. If the terms of an open-end credit plan do not provide for any repayment period, the limitations in paragraph (d)(1)(i) of this section apply to all periods of the credit plan.

(2) **Negative amortization.** A payment schedule with regular periodic payments that cause the principal balance to increase.

(3) **Advance payments.** A payment schedule that consolidates more than two periodic payments and pays them in advance from the proceeds.

(4) **Increased interest rate.** An increase in the interest rate after default.

(5) **Rebates.** A refund calculated by a method less favorable than the actuarial method (as defined by section 933(d) of the Housing and Community Development Act of 1992, 15 U.S.C. 1615(d)), for rebates of interest arising from a loan acceleration due to default.

(6) **Prepayment penalties.** A prepayment penalty, as defined in paragraph (b)(6) of this section.

(7) [Reserved]

(8) **Acceleration of debt.** A demand feature that permits the creditor to accelerate the indebtedness by terminating the high-cost mortgage in advance of the original maturity date and to demand repayment of the entire outstanding balance, except in the following circumstances:

(i) There is fraud or material misrepresentation by the consumer in connection with the loan or open-end credit agreement;

(ii) The consumer fails to meet the repayment terms of the agreement for any outstanding balance that results in a default in payment under the loan; or

(iii) There is any action or inaction by the consumer that adversely affects the creditor's security for the loan, or any right of the creditor in such security.

Regulatory Commentary

Paragraph 32(d) Limitations

1. ***Additional prohibitions applicable under other sections.*** *Section 1026.34 sets forth certain prohibitions in connection with high-cost mortgages, in addition to the limitations in §1026.32(d). Further, §1026.35(b) prohibits certain practices in connection with closed-end transactions that meet the coverage test in §1026.35(a). Because the coverage test in §1026.35(a) is generally broader than the coverage test in §1026.32(a), most closed-end high-cost mortgages are also subject to the prohibitions set forth in §1026.35(b) (such as escrows), in addition to the limitations in §1026.32(d).*

32(d)(1)(i) Balloon Payment

1. ***Regular periodic payments.*** *The repayment schedule for a high-cost mortgage must fully amortize the outstanding principal balance through "regular periodic payments." A payment is a "regular periodic payment" if it is not more than two times the amount of other payments. For*

purposes of open-end credit plans, the term "regular periodic payment" or "periodic payment" means the required minimum periodic payment.

2. ***Repayment period.*** *If the terms of an open-end credit plan provide for a repayment period during which no further draws may be taken, the limitations in §1026.32(d)(1)(i) apply to regular periodic payments required by the credit plan during the draw period, but do not apply to any adjustment in the regular periodic payment that results from the transition from the credit plan's draw period to its repayment period. Further, the limitation on balloon payments in §1026.32(d)(1)(i) does not preclude increases in regular periodic payments that result solely from the initial draw or additional draws on the credit line during the draw period.*

3. ***No repayment period.*** *If the terms of an open-end credit plan do not provide for a repayment period, the repayment schedule must fully amortize any outstanding principal balance in the draw period through regular periodic payments. However, the limitation on balloon payments in §1026.32(d)(1)(i) does not preclude increases in regular periodic payments that result solely from the initial draw or additional draws on the credit line during the draw period.*

32(d)(2) Negative Amortization

1. ***Negative amortization.*** *The prohibition against negative amortization in a high-cost mortgage does not preclude reasonable increases in the principal balance that result from events permitted by the legal obligation unrelated to the payment schedule. For example, when a consumer fails to obtain property insurance and the creditor purchases insurance, the creditor may add a reasonable premium to the consumer's principal balance, to the extent permitted by applicable law and the consumer's legal obligation.*

32(d)(4) Increased Interest Rate

1. ***Variable-rate transactions.*** *The limitation on interest rate increases does not apply to rate increases resulting from changes in accordance with the legal obligation in a variable-rate transaction, even if the increase occurs after default by the consumer.*

32(d)(5) Rebates

1. ***Calculation of refunds.*** *The limitation applies only to refunds of precomputed (such as add-on) interest and not to any other charges that are considered finance charges under §1026.4 (for example, points and fees paid at closing). The calculation of the refund of interest includes odd-days interest, whether paid at or after consummation.*

32(d)(8) Acceleration of debt

Paragraph 32(d)(8)(i)

1. ***Fraud or material misrepresentation.*** *A creditor may terminate a loan or open-end credit agreement and accelerate the balance if there has been fraud or material misrepresentation by the consumer in connection with the loan or open-end credit agreement. What constitutes fraud or misrepresentation is determined by applicable State law and may include acts of omission as well as overt acts, as long as any necessary intent on the part of the consumer exists.*

Paragraph 32(d)(8)(ii)

1. ***Failure to meet repayment terms.*** *A creditor may terminate a loan or open-end credit agreement and accelerate the balance when the consumer fails to meet the repayment terms resulting in a default in payment under the agreement; a creditor may do so, however, only if the consumer actually fails to make payments resulting in a default in the agreement. For example, a creditor may not terminate and accelerate if the consumer, in error, sends a payment to the wrong location, such as a branch rather than the main office of the creditor. If a consumer files for or is placed in bankruptcy, the creditor may terminate and accelerate under §1026.32(d)(8)(ii) if the consumer fails to meet the repayment terms resulting in a default of the agreement. Section 1026.32(d)(8)(ii) does not override any State or other law that requires a creditor to notify a consumer of a right to cure, or otherwise places a duty on the creditor before it can terminate a loan or open-end credit agreement and accelerate the balance.*

Paragraph 32(d)(8)(iii)

1. ***Impairment of security.*** *A creditor may terminate a loan or open-end credit agreement and accelerate the balance if the consumer's action or inaction adversely affects the creditor's security for the loan, or any right of the creditor in that security. Action or inaction by third parties does not, in itself, permit the creditor to terminate and accelerate.*

2. ***Examples.***

i. A creditor may terminate and accelerate, for example, if:

A. The consumer transfers title to the property or sells the property without the permission of the creditor.

B. The consumer fails to maintain required insurance on the dwelling.

C. The consumer fails to pay taxes on the property.

D. The consumer permits the filing of a lien senior to that held by the creditor.

E. The sole consumer obligated on the credit dies.

F. The property is taken through eminent domain.

G. A prior lienholder forecloses.

ii. By contrast, the filing of a judgment against the consumer would be cause for termination and acceleration only if the amount of the judgment and collateral subject to the judgment is such that the creditor's security is adversely and materially affected in violation of the loan or open-end credit agreement. If the consumer commits waste or otherwise destructively uses or fails to maintain the property, including demolishing or removing structures from the property, such that the action adversely affects the security in a material way, the loan or open-end credit agreement may be terminated and the balance accelerated. Illegal use of the property by the consumer would permit termination and acceleration if it subjects the property to seizure. If one of two consumers obligated on a loan dies, the creditor may terminate the loan and accelerate the balance if the security is adversely affected. If the consumer moves out of the dwelling that secures the loan and that action adversely affects the security in a material way, the creditor may terminate a loan or open-end credit agreement and accelerate the balance.

Requirements for Reverse Mortgages

Section 1: Definitions and Disclosure Content
12 C.F.R. § 1026.33(a) and 12 C.F.R. § 1026.33(b)

Definition - 12 CFR § 1026.33(a)]

Discussion

We have elected to not offer a discussion of this section.

Regulatory Text

(a) **Definition.** For purposes of this subpart, *reverse mortgage transaction* means a nonrecourse consumer credit obligation in which:

(1) A mortgage, deed of trust, or equivalent consensual security interest securing one or more advances is created in the consumer's principal dwelling; and

(2) Any principal, interest, or shared appreciation or equity is due and payable (other than in the case of default) only after:

(i) The consumer dies;

(ii) The dwelling is transferred; or

(iii) The consumer ceases to occupy the dwelling as a principal dwelling.

Regulatory Commentary

33(a) Definition

*1. **Nonrecourse transaction.** A nonrecourse reverse mortgage transaction limits the homeowner's liability to the proceeds of the sale of the home (or any lesser amount specified in the credit obligation). If a transaction structured as a closed-end reverse mortgage transaction allows recourse against the consumer, and the annual percentage rate or the points and fees exceed those specified under §1026.32(a)(1), the transaction is subject to all the requirements of §1026.32, including the limitations concerning balloon payments and negative amortization.*

Paragraph 33(a)(2)

*1. **Default.** Default is not defined by the statute or regulation, but rather by the legal obligation between the parties and state or other law.*

*2. **Definite term or maturity date.** To meet the definition of a reverse mortgage transaction, a creditor cannot require any principal, interest, or shared appreciation or equity to be due and payable (other than in the case of default) until after the consumer's death, transfer of the* *dwelling, or the consumer ceases to occupy the dwelling as a principal dwelling. Some state laws require legal obligations secured by a mortgage to specify a definite maturity date or term of repayment in the instrument. An obligation may state a definite maturity date or term of repayment and still meet the definition of a reverse-mortgage transaction if the maturity date or term of repayment used would not operate to cause maturity prior to the occurrence of any of the maturity events recognized in the regulation. For example, some reverse mortgage programs specify that the final maturity date is the borrower's 150th birthday; other programs include a shorter term but provide that the term is automatically extended for consecutive periods if none of the other maturity events has yet occurred. These programs would be permissible.*

Content of Disclosures - 12 CFR § 1026.33(b)]

Discussion

We have elected to not offer a discussion of this section.

Regulatory Text

(b) **Content of disclosures.** In addition to other disclosures required by this part, in a reverse mortgage transaction the creditor shall provide the following disclosures in a form substantially similar to the model form found in paragraph (d) of appendix K of this part:

(1) **Notice.** A statement that the consumer is not obligated to complete the reverse mortgage transaction merely because the consumer has received the disclosures required by this section or has signed an application for a reverse mortgage loan.

(2) **Total annual loan cost rates.** A good-faith projection of the total cost of the credit, determined in accordance with paragraph (c) of this section and expressed as a table of "total annual loan cost rates," using that term, in accordance with appendix K of this part.

(3) **Itemization of pertinent information.** An itemization of loan terms, charges, the age of the youngest borrower and the appraised property value.

(4) **Explanation of table.** An explanation of the table of total annual loan cost rates as provided in the model form found in paragraph (d) of appendix K of this part.

Regulatory Commentary

None.

Section 2: Projected Total Cost of Credit
12 C.F.R. § 1026.33(c)

Projected Total Cost of Credit - 12 C.F.R. § 1026.33(c)

Discussion

We have elected to not offer a discussion of this section.

Regulatory Text

(c) **Projected total cost of credit.** The projected total cost of credit shall reflect the following factors, as applicable:

(1) **Costs to consumer.** All costs and charges to the consumer, including the costs of any annuity the consumer purchases as part of the reverse mortgage transaction.

(2) **Payments to consumer.** All advances to and for the benefit of the consumer, including annuity payments that the consumer will receive from an annuity that the consumer purchases as part of the reverse mortgage transaction.

(3) **Additional creditor compensation.** Any shared appreciation or equity in the dwelling that the creditor is entitled by contract to receive.

(4) **Limitations on consumer liability.** Any limitation on the consumer's liability (such as nonrecourse limits and equity conservation agreements).

(5) **Assumed annual appreciation rates**. Each of the following assumed annual appreciation rates for the dwelling:

(i) 0 percent.

(ii) 4 percent.

(iii) 8 percent.

(6) **Assumed loan period.**

(i) Each of the following assumed loan periods, as provided in appendix L of this part:

(A) Two years.

(B) The actuarial life expectancy of the consumer to become obligated on the reverse mortgage transaction (as of that consumer's most recent birthday). In the case of multiple consumers, the period shall be the actuarial life expectancy of the youngest consumer (as of that consumer's most recent birthday).

(C) The actuarial life expectancy specified by paragraph (c)(6)(i)(B) of this section, multiplied by a factor of 1.4 and rounded to the nearest full year.

(ii) At the creditor's option, the actuarial life expectancy specified by paragraph (c)(6)(i)(B) of this section, multiplied by a factor of .5 and rounded to the nearest full year.

Regulatory Commentary

33(c) Projected Total Cost of Credit

33(c)(1) Costs to Consumer

1. ***Costs and charges to consumer - relation to finance charge.*** *All costs and charges to the consumer that are incurred in a reverse mortgage transaction are included in the projected total cost of credit, and thus in the total annual loan cost rates, whether or not the cost or charge is a finance charge under §1026.4.*

2. ***Annuity costs.*** *As part of the credit transaction, some creditors require or permit a consumer to purchase an annuity that immediately—or at some future time—supplements or replaces the creditor's payments. The amount paid by the consumer for the annuity is a cost to the consumer under this section, regardless of whether the annuity is purchased through the creditor or a third party, or whether the purchase is mandatory or voluntary. For example, this includes the costs of an annuity that a creditor offers, arranges, assists the consumer in purchasing, or that the creditor is aware the consumer is purchasing as a part of the transaction.*

3. ***Disposition costs excluded.*** *Disposition costs incurred in connection with the sale or transfer of the property subject to the reverse mortgage are not included in the costs to the consumer under this paragraph. (However, see the definition of* Val_n *in appendix K to the regulation to determine the effect certain disposition costs may have on the total annual loan cost rates.)*

Paragraph 33(c)(2) Payments to Consumer

1. ***Payments upon a specified event.*** *The projected total cost of credit should not reflect contingent payments in which a credit to the outstanding loan balance or a payment to the consumer's estate is made upon the occurrence of an event (for example, a "death benefit" payable if the consumer's death occurs within a certain period of time). Thus, the table of total annual loan cost rates required under §1026.33(b)(2) would not reflect such payments. At its option, however, a creditor may put an asterisk, footnote, or similar type of notation in the table next to the applicable total annual loan cost rate, and state in the body of the note, apart from the table, the assumption upon which the total annual loan cost is made and any different rate that would apply if the contingent benefit were paid.*

33(c)(3) Additional Creditor Compensation

1. ***Shared appreciation or equity.*** *Any shared appreciation or equity that the creditor is entitled to receive pursuant to the legal obligation must be included in the total cost of a reverse mortgage loan. For example, if a creditor agrees to a reduced interest rate on the transaction in exchange for a portion of the appreciation or equity that may be realized when the dwelling is sold, that portion is included in the projected total cost of credit.*

33(c)(4) Limitations on Consumer Liability

1. ***In general.*** *Creditors must include any limitation on the consumer's liability (such as a nonrecourse limit or an equity conservation agreement) in the projected total cost of credit. These limits and agreements protect a portion of the equity in the dwelling for the consumer or the consumer's estate. For example, the following are limitations on the consumer's liability that must be included in the projected total cost of credit:*

   i. A limit on the consumer's liability to a certain percentage of the projected value of the home.

   ii. A limit on the consumer's liability to the net proceeds from the sale of the property subject to the reverse mortgage.

2. ***Uniform assumption for "net proceeds" recourse limitations.*** *If the legal obligation between the parties does not specify a percentage for the "net proceeds" liability of the consumer, for purposes of the disclosures required by* ***§1026.33****, a creditor must assume that the costs associated with selling the property will equal 7 percent of the projected sale price (see the definition of the* Val_n *symbol under appendix K(b)(6)).*

Prohibited Acts or Practices in Connection with High-Cost (HOEPA) Mortgages

Section 1: Prohibited Acts or Practices for High-Cost Mortgages 12 C.F.R. § 1026.34(a)

Home Improvement Contracts - 12 CFR § 1026.34(a)(1)

Regulatory Discussion

With respect to a high-cost mortgage, a creditor is generally prohibited from paying a contractor other than by one of the following three methods:

- The payment is made either to the consumer, or
- Jointly to both the consumer(s) primarily obligated on the note and the contractor; or
- The payment is made through a third-party escrow agent subject to a written agreement

Regulatory Text

(1) **Home improvement contracts.** A creditor shall not pay a contractor under a home improvement contract from the proceeds of a high-cost mortgage, other than:

(i) By an instrument payable to the consumer or jointly to the consumer and the contractor; or

(ii) At the election of the consumer, through a third-party escrow agent in accordance with terms established in a written agreement signed by the consumer, the creditor, and the contractor prior to the disbursement.

Regulatory Commentary

Paragraph 34(a)(1)(i)

*1. **Joint payees**. If a creditor pays a contractor with an instrument jointly payable to the contractor and the consumer, the instrument must name as payee each consumer who is primarily obligated on the note.*

Notice to Assignee - 12 CFR § 1026.34(a)(2)

Regulatory Discussion

With respect to a high-cost mortgage, a creditor is generally prohibited from selling or otherwise assigning the mortgage without furnishing a prescribed statement to the purchaser or assignee of the fact they may be liable for claims and defenses the consumer could assert against the creditor. The statement must be prominent: i.e., placing it on the face of the note.

Regulatory Text

(2) **Notice to assignee.** A creditor may not sell or otherwise assign a high-cost mortgage without furnishing the following statement to the purchaser or assignee: "Notice: This is a mortgage subject to special rules under the Federal Truth in Lending Act. Purchasers or assignees of this mortgage could be liable for all claims and defenses with respect to the mortgage that the consumer could assert against the creditor."

Regulatory Commentary

34(a)(2) Notice to Assignee

1. ***Subsequent sellers or assignors.*** *Any person, whether or not the original creditor, that sells or assigns a mortgage subject to §1026.32 must furnish the notice of potential liability to the purchaser or assignee.*
2. ***Format.*** *While the notice of potential liability need not be in any particular format, the notice must be prominent. Placing it on the face of the note, such as with a stamp, is one means of satisfying the prominence requirement.*
3. ***Assignee liability***. *Pursuant to section 131(d) of the Act, the Act's general holder-in-due course protections do not apply to purchasers and assignees of loans covered by §1026.32. For such loans, a purchaser's or other assignee's liability for all claims and defenses that the consumer could assert against the creditor is not limited to violations of the Act.*

Refinancings Within One-Year Period - 12 CFR § 1026.34(a)(3)

Regulatory Discussion

With respect to a high-cost mortgage:

- a creditor (or assignee holding or servicinig the mortgage) is generally prohibited from refinancing the mortgage (within one year following the date of origination) to the same consumer into another high-cost mortgage, unless the refinancing is in the consumer's interest.

- a creditor (or assignee) is also prohibited from engaging in acts or practices to evade this provision, including a pattern or practice of arranging for the refinancing of its own loans by affiliated or unaffiliated creditors

The commentary explains what is meant by “in the consumer’s (borrower’s) interest as well as application of the one-year financing prohibition.

Regulatory Text

(3) **Refinancings within one-year period.** Within one year of having extended a high-cost mortgage, a creditor shall not refinance any high-cost mortgage to the same consumer into another high-cost mortgage, unless the refinancing is in the consumer's interest. An assignee holding or servicing a high-cost mortgage shall not, for the remainder of the one-year period following the date of origination of the credit, refinance any high-cost mortgage to the same consumer into another high-cost mortgage, unless the refinancing is in the consumer's interest. A creditor (or assignee) is prohibited from engaging in acts or practices to evade this provision, including a pattern or practice of arranging for the refinancing of its own loans by affiliated or unaffiliated creditors.

Regulatory Commentary

34(a)(3) Refinancings Within One-Year Period

1. ***In the borrower's interest.*** *The determination of whether or not a refinancing covered by §1026.34(a)(3) is in the borrower's interest is based on the totality of the circumstances, at the time the credit is extended. A written statement by the borrower that “this loan is in my interest” alone does not meet this standard.*

   i. A refinancing would be in the borrower's interest if needed to meet the borrower's “bona fide personal financial emergency” (see generally §1026.23(e) and §1026.31(c)(1)(iii)).

   ii. In connection with a refinancing that provides additional funds to the borrower, in determining whether a loan is in the borrower's interest consideration should be given to whether the loan fees and charges are commensurate with the amount of new funds advanced, and whether the real estate-related charges are bona fide and reasonable in amount (see generally §1026.4(c)(7)).

2. ***Application of the one-year refinancing prohibition to creditors and assignees.*** *The prohibition in §1026.34(a)(3) applies where an extension of credit subject to §1026.32 is refinanced into another loan subject to §1026.32. The prohibition is illustrated by the following examples. Assume that Creditor A makes a loan subject to §1026.32 on January 15, 2003, secured by a first lien; this loan is assigned to Creditor B on February 15, 2003:*

   i. Creditor A is prohibited from refinancing the January 2003 loan (or any other loan subject to §1026.32 to the same borrower) into a loan subject to §1026.32, until January 15, 2004. Creditor B is restricted until January 15, 2004, or such date prior to January 15, 2004 that Creditor B ceases to hold or service the loan. During the prohibition period, Creditors A and B may make a subordinate lien loan that does not refinance a loan subject to §1026.32.

Assume that on April 1, 2003, Creditor A makes but does not assign a second-lien loan subject to §1026.32. In that case, Creditor A would be prohibited from refinancing either the first-lien or second-lien loans (or any other loans to that borrower subject to §1026.32) into another loan subject to §1026.32 until April 1, 2004.

ii. The loan made by Creditor A on January 15, 2003 (and assigned to Creditor B) may be refinanced by Creditor C at any time. If Creditor C refinances this loan on March 1, 2003 into a new loan subject to §1026.32, Creditor A is prohibited from refinancing the loan made by Creditor C (or any other loan subject to §1026.32 to the same borrower) into another loan subject to §1026.32 until January 15, 2004. Creditor C is similarly prohibited from refinancing any loan subject to §1026.32 to that borrower into another until March 1, 2004. (The limitations of §1026.34(a)(3) no longer apply to Creditor B after Creditor C refinanced the January 2003 loan and Creditor B ceased to hold or service the loan.)

Repayment Ability for High Cost Mortgages - 12 CFR § 1026.34(a)(4)

Regulatory Discussion

With respect to an <u>open-end</u> high-cost mortgage, a creditor is prohibited from opening an <u>open-end plan</u> without regard to the consumer's repayment ability as described in items (4)(i) through (iv), below. NOTE: temporary or "bridge" loans with terms of twelve months or less, are exempt from this repayment ability requirement.

Substantial commentary is provided on each of the items, (4)(i) through (iv).

With respect to a <u>closed-end</u> high-cost mortgage, a creditor must comply with the repayment ability requirements set forth in §1026.43.

Regulatory Text

(4) **Repayment ability for high-cost mortgages.** In connection with an open-end, high-cost mortgage, a creditor shall not open a plan for a consumer where credit is or will be extended without regard to the consumer's repayment ability as of account opening, including the consumer's current and reasonably expected income, employment, assets other than the collateral, and current obligations including any mortgage-related obligations that are required by another credit obligation undertaken prior to or at account opening, and are secured by the same dwelling that secures the high-cost mortgage transaction. The requirements set forth in §1026.34(a)(4)(i) through (iv) apply to open-end high-cost mortgages, but do not apply to closed-end high-cost mortgages. In connection with a closed-end, high-cost mortgage, a creditor must comply with the repayment ability requirements set forth in §1026.43. Temporary or "bridge" loans with terms of twelve months or less, such as a loan to purchase a new dwelling where the consumer plans to sell a current dwelling within twelve months, are exempt from this repayment ability requirement.

(i) **Mortgage-related obligations.** For purposes of this paragraph (a)(4), mortgage-related obligations are property taxes; premiums and similar charges identified in

§1026.4(b)(5), (7), (8), and (10) that are required by the creditor; fees and special assessments imposed by a condominium, cooperative, or homeowners association; ground rent; and leasehold payments.

(ii) **Basis for determination of repayment ability.** Under this paragraph (a)(4) a creditor must determine the consumer's repayment ability in connection with an open-end, high cost mortgage as follows:

(A) A creditor must verify amounts of income or assets that it relies on to determine repayment ability, including expected income or assets, by the consumer's Internal Revenue Service Form W-2, tax returns, payroll receipts, financial institution records, or other third-party documents that provide reasonably reliable evidence of the consumer's income or assets.

(B) A creditor must verify the consumer's current obligations, including any mortgage-related obligations that are required by another credit obligation undertaken prior to or at account opening, and are secured by the same dwelling that secures the high-cost mortgage transaction.

(iii) **Presumption of compliance.** For an open-end, high cost mortgage, a creditor is presumed to have complied with this paragraph (a)(4) with respect to a transaction if the creditor:

(A) Determines the consumer's repayment ability as provided in paragraph (a)(4)(ii);

(B) Determines the consumer's repayment ability taking into account current obligations and mortgage-related obligations as defined in paragraph (a)(4)(i) of this section, and using the largest required minimum periodic payment based on the following assumptions:

(1) The consumer borrows the full credit line at account opening with no additional extensions of credit;

(2) The consumer makes only required minimum periodic payments during the draw period and any repayment period;

(3) If the annual percentage rate may increase during the plan, the maximum annual percentage rate that is included in the contract, as required by §1026.30, applies to the plan at account opening and will apply during the draw period and any repayment period.

(C) Assesses the consumer's repayment ability taking into account at least one of the following: The ratio of total current obligations, including any mortgage-related obligations that are required by another credit obligation undertaken prior to or at account opening, and are secured by the same dwelling that secures the high-cost mortgage transaction, to income, or the income the consumer will have after paying current obligations.

(iv) **Exclusions from presumption of compliance.** Notwithstanding the previous paragraph, no presumption of compliance is available for an open-end, high-cost mortgage transaction for which the regular periodic payments when aggregated do not fully amortize the outstanding principal balance except as otherwise provided by §1026.32(d)(1)(ii).

Regulatory Commentary

Paragraph 34(a)(4) Repayment Ability for High-Cost Mortgages

1. ***Application of repayment ability rule.*** *The §1026.34(a)(4) prohibition against making loans without regard to consumers' repayment ability applies to open-end, high-cost mortgages. The §1026.43 repayment ability provisions apply to closed-end, high-cost mortgages. Accordingly, in connection with a closed-end, high-cost mortgage, §1026.34(a)(4) requires a creditor to comply with the repayment ability requirements set forth in §1026.43.*

2. ***General prohibition.*** *Section 1026.34(a)(4) prohibits a creditor from extending credit under a high-cost, open-end credit plan based on the value of the consumer's collateral without regard to the consumer's repayment ability as of account opening, including the consumer's current and reasonably expected income, employment, assets other than the collateral, current obligations, and property tax and insurance obligations. A creditor may base its determination of repayment ability on current or reasonably expected income from employment or other sources, on assets other than the collateral, or both.*

3. ***Other dwelling-secured obligations.*** *For purposes of §1026.34(a)(4), current obligations include another credit obligation of which the creditor has knowledge undertaken prior to or at account opening and secured by the same dwelling that secures the high-cost mortgage transaction.*

4. ***Discounted introductory rates and non-amortizing payments.*** *A credit agreement may determine a consumer's initial payments using a temporarily discounted interest rate or permit the consumer to make initial payments that are non-amortizing. In such cases the creditor may determine repayment ability using the assumptions provided in §1026.34(a)(4)(iv).*

5. ***Repayment ability as of account opening.*** *Section 1026.34(a)(4) prohibits a creditor from disregarding repayment ability based on the facts and circumstances known to the creditor as of account opening. In general, a creditor does not violate this provision if a consumer defaults because of a significant reduction in income (for example, a job loss) or a significant obligation (for example, an obligation arising from a major medical expense) that occurs after account opening. However, if a creditor has knowledge as of account opening of reductions in income (for example, if a consumer's written application states that the consumer plans to retire within twelve months without obtaining new employment, or states that the consumer will transition from full-time to part-time employment), the creditor must consider that information.*

6. ***Income, assets, and employment.*** *Any current or reasonably expected assets or income may be considered by the creditor, except the collateral itself. For example, a creditor may use information about current or expected salary, wages, bonus pay, tips, and commissions. Employment may be full-time, part-time, seasonal, irregular, military, or self-employment. Other sources of income could include interest or dividends; retirement benefits; public assistance; and alimony, child support, or separate maintenance payments. A creditor may also take into account assets such as savings accounts or investments that the consumer can or will be able to use.*

7. ***Interaction with Regulation B.*** *Section 1026.34(a)(4) does not require or permit the creditor to make inquiries or verifications that would be prohibited by Regulation B, 12 CFR part 1002.*

34(a)(4)(i) Mortgage-Related Obligations

1. ***Mortgage-related obligations.*** *A creditor must include in its repayment ability analysis the expected property taxes and premiums for mortgage-related insurance required by the creditor as set forth in §1026.35(b), as well as similar mortgage-related expenses. Similar mortgage-related expenses include homeowners' association dues and condominium or cooperative fees.*

34(a)(4)(ii) Verification of Repayment Ability

1. ***Income and assets relied on.*** *A creditor must verify the income and assets the creditor relies on to evaluate the consumer's repayment ability. For example, if a consumer earns a salary and also states that he or she is paid an annual bonus, but the creditor only relies on the applicant's salary to evaluate repayment ability, the creditor need only verify the salary.*
2. ***Income and assets – no co-applicant.*** *If two persons jointly apply for credit and both list income or assets on the application, the creditor must verify repayment ability with respect to both applicants unless the creditor relies only on the income or assets of one of the applicants in determining repayment ability.*
3. ***Expected income.*** *If a creditor relies on expected income, the expectation must be reasonable and it must be verified with third-party documents that provide reasonably reliable evidence of the consumer's expected income. For example, if the creditor relies on an expectation that a consumer will receive an annual bonus, the creditor may verify the basis for that expectation with documents that show the consumer's past annual bonuses and the expected bonus must bear a reasonable relationship to past bonuses. Similarly, if the creditor relies on a consumer's expected salary following the consumer's receipt of an educational degree, the creditor may verify that expectation with a written statement from an employer indicating that the consumer will be employed upon graduation at a specified salary.*

Paragraph 34(a)(4)(ii)(A)

1. ***Internal Revenue Service (IRS) Form W-2.*** *A creditor may verify a consumer's income using a consumer's IRS Form W-2 (or any subsequent revisions or similar IRS Forms used for reporting wages and tax withholding). The creditor may also use an electronic retrieval service for obtaining the consumer's W-2 information.*
2. ***Tax returns.*** *A creditor may verify a consumer's income or assets using the consumer's tax return. A creditor may also use IRS Form 4506 "Request for Copy of Tax Return," Form 4506-T "Request for Transcript of Tax Return," or Form 8821 "Tax Information Authorization" (or any subsequent revisions or similar IRS Forms appropriate for obtaining tax return information directly from the IRS) to verify the consumer's income or assets. The creditor may also use an electronic retrieval service for obtaining tax return information.*
3. ***Other third-party documents that provide reasonably reliable evidence of consumer's income or assets.*** *Creditors may verify income and assets using documents produced by third parties. Creditors may not rely on information provided orally by third parties, but may rely on correspondence from the third party, such as by letter or email. The creditor may rely on any third-party document that provides reasonably reliable evidence of the consumer's income or assets. For example, creditors may verify the consumer's income using receipts from a check-cashing or remittance service, or by obtaining a written statement from the consumer's employer that states the consumer's income.*

4. ***Information specific to the consumer.*** *Creditors must verify a consumer's income or assets using information that is specific to the individual consumer. Creditors may use third-party databases that contain individual-specific data about a consumer's income or assets, such as a third-party database service used by the consumer's employer for the purpose of centralizing income verification requests, so long as the information is reasonably current and accurate. Information about average incomes for the consumer's occupation in the consumer's geographic location or information about average incomes paid by the consumer's employer, however, would not be specific to the individual consumer.*

5. ***Duplicative collection of documentation.*** *A creditor that has made a loan to a consumer and is refinancing or extending new credit to the same consumer need not collect from the consumer a document the creditor previously obtained if the creditor has no information that would reasonably lead the creditor to believe that document has changed since it was initially collected. For example, if the creditor has obtained the consumer's 2006 tax return to make a home purchase loan in May 2007, the creditor may rely on the 2006 tax return if the creditor makes a home equity loan to the same consumer in August 2007. Similarly, if the creditor has obtained the consumer's bank statement for May 2007 in making the first loan, the creditor may rely on that bank statement for that month in making the subsequent loan in August 2007.*

Paragraph 34(a)(4)(ii)(B)

1. ***In general.*** *A credit report may be used to verify current obligations. A credit report, however, might not reflect an obligation that a consumer has listed on an application. The creditor is responsible for considering such an obligation, but the creditor is not required to independently verify the obligation. Similarly, a creditor is responsible for considering certain obligations undertaken just before or at account opening and secured by the same dwelling that secures the transaction (for example, a "piggy back" loan), of which the creditor knows, even if not reflected on a credit report. See comment 34(a)(4)-3.*

34(a)(4)(iii) Presumption of Compliance

1. ***In general.*** *A creditor is presumed to have complied with §1026.34(a)(4) if the creditor follows the three underwriting procedures specified in paragraph 34(a)(4)(iii) for verifying repayment ability, determining the payment obligation, and measuring the relationship of obligations to income. The procedures for verifying repayment ability are required under §1026.34(a)(4)(ii); the other procedures are not required but, if followed along with the required procedures, create a presumption that the creditor has complied with §1026.34(a)(4). The consumer may rebut the presumption with evidence that the creditor nonetheless disregarded repayment ability despite following these procedures. For example, evidence of a very high debt-to-income ratio and a very limited residual income could be sufficient to rebut the presumption, depending on all of the facts and circumstances. If a creditor fails to follow one of the non-required procedures set forth in §1026.34(a)(4)(iii), then the creditor's compliance is determined based on all of the facts and circumstances without there being a presumption of either compliance or violation.*

Paragraph 34(a)(4)(iii)(B)

1. ***Determination of payment schedule.*** *To retain a presumption of compliance under §1026.34(a)(4)(iii), a creditor must determine the consumer's ability to pay the principal and*

interest obligation based on the maximum scheduled payment. In general, a creditor should determine a payment schedule for purposes of §1026.34(a)(4)(iii)(B) based on the guidance in the commentary to §1026.32(c)(3).

Paragraph 34(a)(4)(iii)(C)

1. ***"Income" and "debt".*** *To determine whether to classify particular inflows or obligations as "income" or "debt," creditors may look to widely accepted governmental and non-governmental underwriting standards, including, for example, those set forth in the Federal Housing Administration's handbook on Mortgage Credit Analysis for Mortgage Insurance.*

34(a)(4)(iv) Exclusions From Presumption of Compliance

1. ***In general.*** *The exclusions from the presumption of compliance should be interpreted consistent with comments 32(d)(1)(i)-1 and 32(d)(2)-1.*

2. ***Renewable balloon loan.*** *If a creditor is unconditionally obligated to renew a balloon-payment loan at the consumer's option (or is obligated to renew subject to conditions within the consumer's control), the full term resulting from such renewal is the relevant term for purposes of the exclusion of certain balloon-payment loans. See comment 17(c)(1)-11 for a discussion of conditions within a consumer's control in connection with renewable balloon-payment loans.*

Pre-Loan Counseling - 12 CFR § 1026.34(a)(5)

Regulatory Discussion

With respect to a high-cost mortgage, a creditor is prohibited from extending a high-cost mortgage unless:

- the creditor has received written certification the consumer has obtained counseling, subject to the following conditions:
- the counseling must occur after either of the two events described in (5)(ii)(A) and (B), below
- the counseling was not provided by a counselor employed or affiliated with the creditor (5)(iii), below
- the certification of counseling must include six specific pieces of information described in (5)(iv)(A) through (F), below
- the creditor may pay the fees for the counseling – but may not condition the payment on the consummation or account-opening (5)(v), below
- In the event, the consumer withdraws the application, a creditor may not condition the payment on the receipt of certification required under (a)(5)(i), above; however, the creditor may confirm a counselor has provided counseling prior to paying the fee.
- The creditor may not steer or otherwise direct a consumer to choose a particular counselor (5)(vi), below

Substantial commentary is provided on items (5)(i), (ii), (iv), (v) and (vi).

Regulatory Text

(5) **Pre-loan counseling.**

(i) **Certification of counseling required.** A creditor shall not extend a high-cost mortgage to a consumer unless the creditor receives written certification that the consumer has obtained counseling on the advisability of the mortgage from a counselor that is approved to provide such counseling by the Secretary of the U.S. Department of Housing and Urban Development or, if permitted by the Secretary, by a State housing finance authority.

(ii) **Timing of counseling**. The counseling required under this paragraph (a)(5) must occur after:

(A) The consumer receives either the disclosure required by section 5(c) of the Real Estate Settlement Procedures Act of 1974 (12 U.S.C. 2604(c)) or the disclosures required by §1026.40; or

(B) The consumer receives the disclosures required by §1026.32(c), for transactions in which neither of the disclosures listed in paragraph (a)(5)(ii)(A) of this section are provided.

(iii) **Affiliation prohibited.** The counseling required under this paragraph (a)(5) shall not be provided by a counselor who is employed by or affiliated with the creditor.

(iv) **Content of certification**. The certification of counseling required under paragraph (a)(5)(i) must include:

(A) The name(s) of the consumer(s) who obtained counseling;

(B) The date(s) of counseling;

(C) The name and address of the counselor;

(D) A statement that the consumer(s) received counseling on the advisability of the high-cost mortgage based on the terms provided in either the disclosure required by section 5(c) of the Real Estate Settlement Procedures Act of 1974 (12 U.S.C. 2604(c)) or the disclosures required by §1026.40.

(E) For transactions for which neither of the disclosures listed in paragraph (a)(5)(ii)(A) of this section are provided, a statement that the consumer(s) received counseling on the advisability of the high-cost mortgage based on the terms provided in the disclosures required by §1026.32(c); and

(F) A statement that the counselor has verified that the consumer(s) received the disclosures required by either §1026.32(c) or the Real Estate Settlement Procedures Act of 1974 (12 U.S.C. 2601 *et seq.*) with respect to the transaction.

(v) **Counseling fees.** A creditor may pay the fees of a counselor or counseling organization for providing counseling required under this paragraph (a)(5) but may not condition the payment of such fees on the consummation or account-opening of a mortgage transaction. If the consumer withdraws the application that would result in the extension of a high-cost mortgage, a creditor may not condition the payment of such fees on the receipt of certification from the counselor required by paragraph (a)(5)(i) of this section. A creditor may, however, confirm that a counselor has provided counseling to the consumer pursuant to this paragraph (a)(5) prior to paying the fee of a counselor or counseling organization.

(vi) **Steering prohibited.** A creditor that extends a high-cost mortgage shall not steer or otherwise direct a consumer to choose a particular counselor or counseling organization for the counseling required under this paragraph (a)(5).

Regulatory Commentary

34(a)(5)(i) Certification of counseling required.

1. ***HUD-approved counselor.*** *For purposes of §1026.34(a)(5), counselors approved by the Secretary of the U.S. Department of Housing and Urban Development are homeownership counselors certified pursuant to section 106(e) of the Housing and Urban Development Act of 1968 (12 U.S.C. 1701x(e)), or as otherwise determined by the Secretary.*

2. ***State housing finance authority.*** *For purposes of §1026.34(a)(5), a "State housing finance authority" has the same meaning as "State housing finance agency" provided in 24 CFR 214.3.*

3. ***Processing applications.*** *Prior to receiving certification of counseling, a creditor may not extend a high-cost mortgage, but may engage in other activities, such as processing an application that will result in the extension of a high-cost mortgage (by, for example, ordering an appraisal or title search).*

4. ***Form of certification.*** *The written certification of counseling required by §1026.34(a)(5)(i) may be received by mail, email, facsimile, or any other method, so long as the certification is in a retainable form.*

5. ***Purpose of certification.*** *Certification of counseling indicates that a consumer has received counseling as required by §1026.34(a)(5), but it does not indicate that a counselor has made a judgment or determination as to the appropriateness of the transaction for the consumer.*

34(a)(5)(ii) Timing of counseling.

1. ***Disclosures for open-end credit plans****.* *Section 1026.34(a)(5)(ii) permits receipt of either the disclosure required by section 5(c) of RESPA or the disclosures required under §1026.40 to allow counseling to occur. Pursuant to 12 CFR 1024.7(h), the disclosures required by §1026.40 can be provided for open-end plans in lieu of the usual disclosure required by section 5(c) of RESPA.*

2. ***Transactions not subject to RESPA or §1026.40.*** *For closed-end mortgage transactions that are not subject to RESPA, the counseling certification must include a statement that the consumer(s) received counseling on the advisability of the high-cost mortgage based on the terms provided in the disclosures required by §1026.32(c). (Reference to counseling on advisability using the disclosures required by §1026.32(c) is not required for transactions subject to RESPA or §1026.40.) The disclosures required by §1026.32(c) must be furnished to the consumer at least three business days prior to consummation of the mortgage. The creditor*

may wish to furnish the disclosures sooner, to provide sufficient time for counseling and certification.

3. ***Initial disclosure.*** *Counseling may occur after receipt of either an initial disclosure required by section 5(c) of RESPA, the disclosures required by §1026.40, or the disclosures required by §1026.32(c), regardless of whether revised versions of such disclosures are subsequently provided to the consumer.*

34(a)(5)(iv) Content of certification.

1. ***Statement of counseling on advisability.*** *A statement that a consumer has received counseling on the advisability of the high-cost mortgage means that the consumer has received counseling about key terms of the mortgage transaction, as set out in either the disclosure required by section 5(c) of RESPA or the disclosures provided to the consumer pursuant to §1026.40, or, for closed-end transactions not subject to RESPA, the disclosures required by §1026.32(c); the consumer's budget, including the consumer's income, assets, financial obligations, and expenses; and the affordability of the mortgage transaction for the consumer. Examples of such terms of the mortgage transaction include the initial interest rate, the initial monthly payment, whether the payment may increase, how the minimum periodic payment will be determined, and fees imposed by the creditor, as may be reflected in the applicable disclosure. A statement that a consumer has received counseling on the advisability of the high-cost mortgage does not require the counselor to have made a judgment or determination as to the appropriateness of the mortgage transaction for the consumer.*

2. ***Statement of verification.*** *A statement that a counselor has verified that the consumer has received the disclosures required by either §1026.32(c) or by RESPA for the high-cost mortgage means that a counselor has confirmed, orally, in writing, or by some other means, receipt of such disclosures with the consumer.*

34(a)(5)(v) Counseling fees.

1. ***Financing.*** *Section 1026.34(a)(5)(v) does not prohibit a creditor from financing the counseling fee as part of the transaction for a high-cost mortgage, if the fee is a bona fide third-party charge as provided by §1026.32(b)(5)(i).*

34(a)(5)(vi) Steering prohibited.

1. *An example of an action that constitutes steering would be when a creditor repeatedly highlights or otherwise distinguishes the same counselor in the notices the creditor provides to consumers pursuant to §1026.34(a)(5)(vii).*

2. *Section 1026.34(a)(5)(vi) does not prohibit a creditor from providing a consumer with objective information related to counselors or counseling organizations in response to a consumer's inquiry. An example of an action that would not constitute steering would be when a consumer asks the creditor for information about the fees charged by a counselor, and the creditor responds by providing the consumer information about fees charged by the counselor to other consumers that previously obtained counseling pursuant to §1026.34(a)(5).*

Recommended Default - 12 CFR § 1026.34(a)(6)

Regulatory Discussion

With respect to a high-cost mortgage that refinances all or any portion of an existing loan, a creditor (or mortgage broker) is prohibited from recommending or encouraging default on the existing loan prior to the consummation or account opening of the new high-cost mortgage. The commentary provides examples.

Regulatory Text

(6) **Recommended default.** A creditor or mortgage broker, as defined in section 1026.36(a)(2), may not recommend or encourage default on an existing loan or other debt prior to and in connection with the consummation or account opening of a high-cost mortgage that refinances all or any portion of such existing loan or debt.

Regulatory Commentary

34(a)(6) Recommended default.

1. ***Facts and circumstances.*** *Whether a creditor or mortgage broker "recommends or encourages" default for purposes of §1026.34(a)(6) depends on all of the relevant facts and circumstances.*

2. ***Examples.***

i. A creditor or mortgage broker "recommends or encourages" default when the creditor or mortgage broker advises the consumer to stop making payments on an existing loan in a manner that is likely to cause the consumer to default on the existing loan.

ii. When delay of consummation of a high-cost mortgage occurs for reasons outside the control of a creditor or mortgage broker, that creditor or mortgage broker does not "recommend or encourage" default because the creditor or mortgage broker informed a consumer that:

A. The consumer's high-cost mortgage is scheduled to be consummated prior to the due date for the next payment due on the consumer's existing loan, which is intended to be paid by the proceeds of the new high-cost mortgage; and

B. Any delay of consummation of the new high-cost mortgage beyond the payment due date of the existing loan will not relieve the consumer of the obligation to make timely payment on that loan.

Modification and Deferral Fees - 12 CFR § 1026.34(a)(7)

Regulatory Discussion

With respect to a high-cost mortgage, a creditor, etc., is prohibited from

- charging any fee to modify, renew, extend or amend the high-cost mortgage; or
- deferring any payment due on the high-cost mortgage

Regulatory Text

(7) **Modification and deferral fees.** A creditor, successor-in-interest, assignee, or any agent of such parties may not charge a consumer any fee to modify, renew, extend or amend a high-cost mortgage, or to defer any payment due under the terms of such mortgage.

Regulatory Commentary

None.

Late Fees - 12 CFR § 1026.34(a)(8)

Regulatory Discussion

With respect to a high-cost mortgage, late payment fees are subject to the following four conditions:

- In general, any late charge must be specifically permitted and may not exceed 4% of the amount of the past due payment.
- May only be imposed if the payment is not received by the end of either the applicable 15- or 30-day period.
- May not be imposed if any delinquency is attributable only to a late payment charge imposed on an earlier payment. See the commentary for an example.
- May be imposed for any payment(s) outstanding until the default is cured. See the commentary for an example.

Regulatory Text

(8) **Late fees.**

(i) **General.** Any late payment charge imposed in connection with a high-cost mortgage must be specifically permitted by the terms of the loan contract or open-end credit agreement and may not exceed 4 percent of the amount of the payment past due. No such charge may be imposed more than once for a single late payment.

(ii) **Timing.** A late payment charge may be imposed in connection with a high-cost mortgage only if the payment is not received by the end of the 15-day period beginning on the date the payment is due or, in the case of a high-cost mortgage on which interest on each installment is paid in advance, the end of the 30-day period beginning on the date the payment is due.

(iii) **Multiple late charges assessed on payment subsequently paid.** A late payment charge may not be imposed in connection with a high-cost mortgage payment if any delinquency is attributable only to a late payment charge imposed on an earlier payment, and the payment otherwise is a full payment for the applicable period and is paid by the due date or within any applicable grace period.

(iv) **Failure to make required payment.** The terms of a high-cost mortgage agreement may provide that any payment shall first be applied to any past due balance. 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 payment(s) outstanding (without deduction due to late fees or related fees) until the default is cured.

Regulatory Commentary

34(a)(8)(i) General.

1. For purposes of §1026.34(a)(8), in connection with an open-end credit plan, the amount of the payment past due is the required minimum periodic payment as provided under the terms of the open-end credit agreement.

34(a)(8)(iii) Multiple late charges assessed on payment subsequently paid.

1. Section 1026.34(a)(8)(iii) prohibits the pyramiding of late fees or charges in connection with a high-cost mortgage payment. For example, assume that a consumer's regular periodic payment of $500 is due on the 1st of each month. On August 25, the consumer makes a $500 payment which was due on August 1, and as a result, a $10 late charge is assessed. On September 1, the consumer makes another $500 payment for the regular periodic payment due on September 1, but does not pay the $10 late charge assessed on the August payment. Under §1026.34(h)(2), it is impermissible to allocate $10 of the consumer's September 1 payment to cover the late charge, such that the September payment becomes delinquent. In short, because the $500 payment made on September 1 is a full payment for the applicable period and is paid by its due date or within any applicable grace period, no late charge may be imposed on the account in connection with the September payment.

34(a)(8)(iv) Failure to make required payment.

1. Under §1026.34(a)(8)(iv), if a consumer fails to make one or more required payments and then resumes making payments but fails to bring the account current, it is permissible, if permitted by the terms of the loan contract or open-end credit agreement, to apply the consumer's payments first to the past due payment(s) and to impose a late charge on each subsequent required payment until the account is brought current. To illustrate: Assume that a consumer's regular periodic *payment of $500 is due on the 1st of each month, or before the expiration of a 15-day grace period. Also assume that the consumer fails to make a timely installment payment by August 1 (or within the applicable grace period), and a $10 late charge therefore is imposed. The consumer resumes making monthly payments on September 1. Under §1026.34(a)(8)(iv), if permitted by the terms of the loan contract, the creditor may apply the $500 payment made on September 1 to satisfy the missed $500 payment that was due on August 1. If the consumer makes no other payment prior to the end of the grace period for the payment that was due on September 1, the creditor may also impose a $10 late fee for the payment that was due on September 1.*

Payoff Statements - 12 CFR § 1026.34(a)(9)

Regulatory Discussion

With respect to a high-cost mortgage, in general, a creditor (or servicer) is prohibited from charging a fee for providing a payoff statement. The payoff statement shall be provided within five business days after receiving the request.

Note, however, the creditor (or servicer) may charge a "processing fee" to cover the cost of providing a payoff statement by fax or courier. Prior to charging this "processing fee," the creditor (or servicer) shall disclose to the consumer that the payoff statement is available by a method other than by fax or courier without charge.

In the event more than four payoff statements have been provided in a calendar year, the creditor (or servicer) may thereafter charge a reasonable fee for providing such statements during the remainder of the calendar year. Payoff statements provided to a consumer in a subsequent calendar year are subject to the requirements of this section.

Regulatory Text

(9) **Payoff statements**

(i) **Fee prohibition.** In general, a creditor or servicer (as defined in 12 CFR 1024.2(b)) may not charge a fee for providing to a consumer, or a person authorized by the consumer to obtain such information, a statement of the amount due to pay off the outstanding balance of a high-cost mortgage.

(ii) **Processing fee**. A creditor or servicer may charge a processing fee to cover the cost of providing a payoff statement, as described in paragraph (a)(9)(i) of this section, by fax or courier, provided that such fee may not exceed an amount that is comparable to fees imposed for similar services provided in connection with consumer credit transactions that are secured by the consumer's principal dwelling and are not high-cost mortgages. A creditor or servicer shall make a payoff statement available to a consumer, or a person authorized by the consumer to obtain such information, by a method other than by fax or courier and without charge pursuant to paragraph (a)(9)(i) of this section.

(iii) **Processing fee disclosure.** Prior to charging a processing fee for provision of a payoff statement by fax or courier, as permitted pursuant to paragraph (a)(9)(ii) of this section, a creditor or servicer shall disclose to a consumer or a person authorized by the consumer to obtain the consumer's payoff statement that payoff statements, as described in paragraph (a)(9)(i) of this section, are available by a method other than by fax or courier without charge.

(iv) **Fees permitted after multiple requests**. A creditor or servicer that has provided a payoff statement, as described in paragraph (a)(9)(i) of this section, to a consumer, or a person authorized by the consumer to obtain such information, without charge, other than the processing fee permitted under paragraph (a)(9)(ii) of this section, four times during a calendar year, may thereafter charge a reasonable fee for providing such statements during the remainder of the calendar year. Fees for payoff statements provided to a consumer, or a person authorized by the consumer to obtain such information, in a subsequent calendar year are subject to the requirements of this section.

(v) **Timing of delivery of payoff statements.** A payoff statement, as described in paragraph (a)(9)(i) of this section, for a high-cost mortgage shall be provided by a creditor or servicer within five business days after receiving a request for such statement by a consumer or a person authorized by the consumer to obtain such statement.

Regulatory Commentary

None.

Financing Points and Fees - 12 CFR § 1026.34(a)(10)

Regulatory Discussion

With respect to a high-cost mortgage, a creditor is prohibited from financing charges that are considered "points and fees" as defined in §1026.32(b)(1) and (2). Exception: credit insurance premiums or debt cancellation or suspension fees that are required to be included in points and fees shall not be considered financed by the creditor when they are calculated and paid in full on a monthly basis.

Regulatory Text

(10) **Financing of points and fees.** A creditor that extends credit under a high-cost mortgage may not finance charges that are required to be included in the calculation of points and fees, as that term is defined in §1026.32(b)(1) and (2). Credit insurance premiums or debt cancellation or suspension fees that are required to be included in points and fees under §1026.32(b)(1)(iv) or (2)(iv) shall not be considered financed by the creditor when they are calculated and paid in full on a monthly basis.

Regulatory Commentary

34(a)(10) Financing of points and fees.

1. ***Points and fees.*** *For purposes of §1026.34(a)(10), "points and fees" means those items that are required to be included in the calculation of points and fees under §1026.32(b)(1) and (2). Thus, for example, in connection with the extension of credit under a high-cost mortgage, a creditor may finance a fee charged by a third-party counselor in connection with the consumer's receipt of pre-loan counseling under §1026.34(a)(5), because, pursuant to §1026.32(b)(1)(i)(D) and (b)(2)(i)(D), such a fee is excluded from the calculation of points and fees as a bona fide third-party charge.*

2. ***Examples of financing points and fees.*** *For purposes of §1026.34(a)(10), points and fees are financed if, for example, they are added to the loan balance or financed through a separate note, if the note is payable to the creditor or to an affiliate of the creditor. In the case of an open-end credit plan, a creditor also finances points and fees if the creditor advances funds from the credit line to cover the fees.*

Section 2: Prohibited Acts or Practices for Dwelling Secured Loans; Structuring Loans to Evade High Cost Mortgage Requirements

12 C.F.R. § 1026.34(b)

Prohibited Acts or Practices for Dwelling Secured Loans; Structuring Loans to Evade High Cost Mortgage Requirements - 12 CFR § 1026.34(b)

Regulatory Discussion

With respect to a high-cost mortgage, a creditor is prohibited from structuring a transaction (including dividing any loan into separate parts) with the intent to evade the requirements of this section. See commentary for examples.

Regulatory Text

(b) **Prohibited acts or practices for dwelling-secured loans; structuring loans to evade high-cost mortgage requirements.** A creditor shall not structure any transaction that is otherwise a high-cost mortgage in a form, for the purpose, and with the intent to evade the requirements of a high-cost mortgage subject to this subpart, including by dividing any loan transaction into separate parts.

Regulatory Commentary

34(b) Prohibited acts or practices for dwelling-secured loans; structuring loans to evade high-cost mortgage requirements.

*1. **Examples.***

i. A creditor structures a transaction in violation of §1026.34(b) if, for example, the creditor structures a loan that would otherwise be a high-cost mortgage as two or more loans, whether made consecutively or at the same time, for example, to divide the loan fees to avoid the points and fees threshold for high-cost mortgages in §1026.32(a)(1)(ii).

ii. A creditor does not structure a transaction in violation of §1026.34(b) when a loan to finance the initial construction of a dwelling may be permanently financed by the same creditor, such as a "construction-to-permanent" loan, and the construction phase and the permanent phase are treated as separate transactions. Section 1026.17(c)(6)(ii) permits the creditor to give either one combined disclosure for both the construction financing and the permanent financing, or a separate set of disclosures for each of the two phases as though they were two separate transactions. See also comment 17(c)(6)-2.

*2. **Amount of credit extended.** Where a loan is documented as open-end credit but the features and terms or other circumstances demonstrate that it does not meet the definition of open-end credit, the loan is subject to the rules for closed-end credit. Thus, in determining the "total loan amount" for purposes of applying the triggers under §1026.32, the amount of credit that would have been extended if the loan had been documented as a closed-end loan is a factual determination to be made in each case. Factors to be considered include the amount of money the consumer originally requested, the amount of the first advance or the highest outstanding balance, or the amount of the credit line. The full amount of the credit line is considered only to the extent that it is reasonable to expect that the consumer might use the full amount of credit.*

Requirements for Higher-Priced Mortgage Loans

Section 1: Definitions
12 C.F.R. § 1026.35(a)

Definitions – Higher Priced Mortgage Loan - 12 CFR § 1026.35(a)(1)

Regulatory Discussion

This section defines the term "***higher-priced mortgage.***" There are three types; all must be secured by the consumer's principal dwelling:

- Conventional, first lien;
- Jumbo, first lien;
- Either conventional or jumbo, subordinate lien

Regulatory Text

(a) **Definitions.** For purposes of this section:

(1) **"Higher-priced mortgage loan"** means a closed-end consumer credit transaction secured by the consumer's principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set:

(i) By 1.5 or more percentage points for loans secured by a first lien 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;

(ii) By 2.5 or more percentage points for loans secured by a first lien 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; or

(iii) By 3.5 or more percentage points for loans secured by a subordinate lien.

Regulatory Commentary

Paragraph 35(a)(1)

1. ***Comparable transaction.*** *A higher-priced mortgage loan is a consumer credit transaction secured by the consumer's principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by the specified margin. The table of average prime offer rates published by the Bureau indicates how to identify the comparable transaction.*

2. ***Rate set.*** *A transaction's annual percentage rate is compared to the average prime offer rate as of*

the date the transaction's interest rate is set (or "locked") before consummation. Sometimes a creditor sets the interest rate initially and then re-sets it at a different level before consummation. The creditor should use the last date the interest rate is set before consummation.

3. ***Threshold for "jumbo" loans.*** *Section 1026.35(a)(1)(ii) provides a separate threshold for determining whether a transaction is a higher-priced mortgage loan subject to §1026.35 when the principal balance exceeds the limit in effect as of the date the transaction's rate is set for the maximum principal obligation eligible for purchase by Freddie Mac (a "jumbo" loan). The Federal Housing Finance Agency (FHFA) establishes and adjusts the maximum principal obligation pursuant to rules under 12 U.S.C. 1454(a)(2) and other provisions of federal law. Adjustments to the maximum principal obligation made by FHFA apply in determining whether a mortgage loan is a "jumbo" loan to which the separate coverage threshold in §1026.35(a)(1)(ii) applies.*

Definitions - Average Prime Offer Rate - 12 CFR § 1026.35(a)(2)

Regulatory Discussion

This section defines the term "*average prime offer rate*," ("APOR"). The CFPB publishes the APOR on the Internet and is updated at least weekly.

Regulatory Text

(a) **Definitions.** For purposes of this section:

(2) **"Average prime offer rate"** means an annual percentage rate 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. The Bureau publishes average prime offer rates for a broad range of types of transactions in a table updated at least weekly as well as the methodology the Bureau uses to derive these rates.

Regulatory Commentary

Paragraph 35(a)(2)

1. ***Average prime offer rate.*** *Average prime offer rates are annual percentage rates 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. Other pricing terms include commonly used indices, margins, and initial fixed-rate periods for variable-rate transactions. Relevant pricing characteristics include a consumer's credit history and transaction characteristics such as the loan-to-value ratio, owner-occupant status, and purpose of the transaction. To obtain average prime offer rates, the Bureau uses a survey of creditors that both meets the criteria of §1026.35(a)(2) and provides pricing terms for at least two types of variable-rate transactions and at least two types of non-variable-rate transactions. An example of such a survey is the Freddie Mac Primary Mortgage Market Survey®.*

2. ***Bureau table.*** *The Bureau publishes on the Internet, in table form, average prime offer rates for a wide variety of transaction types. The Bureau calculates an annual percentage rate, consistent with Regulation Z (see §1026.22 and appendix J), for each transaction type for which pricing terms are available from a survey. The Bureau estimates annual percentage rates for other types of transactions for which direct survey data are not available based on the loan pricing terms available in the survey and other information. The Bureau publishes on the Internet the methodology it uses to arrive at these estimates.*

3. ***Additional guidance on determination of average prime offer rates.*** *The average prime offer rate has the same meaning in §1026.35 as in Regulation C, 12 CFR part 1003. See 12 CFR 1003.4(a)(12)(ii). Guidance on the average prime offer rate under §1026.35(a)(2), such as when a transaction's rate is set and determination of the comparable transaction, is provided in the official commentary under Regulation C, the publication entitled "A Guide to HMDA Reporting: Getting it Right!", and the relevant "Frequently Asked Questions" on Home Mortgage Disclosure Act (HMDA) compliance posted on the FFIEC's Web site at http://www.ffiec.gov/hmda.*

Section 2: Escrow Accounts
12 C.F.R. § 1026.35(b)

Escrow Accounts - 12 CFR § 1026.35(b)(1)

Regulatory Discussion

Generally, a first-lien higher-priced mortgage requires an escrow account for payment of property taxes and mortgage-related insurance premiums. The escrow account must be established before consummation.

Note the commentary on: Optional insurance items; and Transactions not subject to this section, (b)(1).

Discussion on escrow account exceptions is found in (b)(2), below.

Regulatory Text

(b) Escrow accounts

(1) **Requirement to escrow for property taxes and insurance.** Except as provided in paragraph (b)(2) of this section, a creditor may not extend a higher-priced mortgage loan secured by a first lien on a consumer's principal dwelling unless an escrow account is established before consummation for payment of property taxes and premiums for mortgage-related insurance required by the creditor, such as insurance against loss of or damage to property, or against liability arising out of the ownership or use of the property, or insurance protecting the creditor against the consumer's default or other credit loss. For purposes of this paragraph (b), the term "escrow account" has the same meaning as under Regulation X (12 CFR 1024.17(b)), as amended.

Regulatory Commentary

35(b) Escrow Accounts

1. ***Principal dwelling.*** *Section 1026.35(b)(1) applies to principal dwellings, including structures that are classified as personal property under State law. For example, an escrow account must be established on a higher-priced mortgage loan secured by a first lien on a manufactured home, boat, or trailer used as the consumer's principal dwelling. See the commentary under §§1026.2(a)(19) and(24), 1026.15, and 1026.23. Section 1026.35(b)(1) also applies to a higher-priced mortgage loan secured by a first lien on a condominium if it is in fact used as the consumer's principal dwelling. But see §1026.35(b)(2) for exemptions from the escrow requirement that may apply to such transactions.*

35(b)(1) Requirement to escrow for property taxes and insurance

*1. **Administration of escrow accounts.** Section 1026.35(b)(1) requires creditors to establish an escrow account for payment of property taxes and premiums for mortgage-related insurance required by the creditor before the consummation of a higher-priced mortgage loan secured by a first lien on a principal dwelling. Section 6 of RESPA, 12 U.S.C. 2605, and Regulation X, 12 CFR 1024.17, address how escrow accounts must be administered.*

*2. **Optional insurance items.** Section 1026.35(b)(1) does not require that an escrow account be established for premiums for mortgage-related insurance that the creditor does not require in connection with the credit transaction, such as earthquake insurance or credit life insurance, even if the consumer voluntarily obtains such insurance.*

*3. **Transactions not subject to §1026.35(b)(1).** Section 1026.35(b)(1) requires a creditor to establish an escrow account before consummation of a first-lien higher-priced mortgage loan. This requirement does not affect a creditor's ability, right, or obligation, pursuant to the terms of the legal obligation or applicable law, to offer or require an escrow account for a transaction that is not subject to §1026.35(b)(1).*

Escrow Accounts - Exemptions - 12 CFR § 1026.35(b)(2)

Regulatory Discussion

There are four categories of escrow account exemptions, as follows:

An escrow account is not required for the following four transaction types (as described in (b)(2)(i)):

- Secured by shares in a cooperative
- Initial construction of a dwelling
- Temporary, or “bridge,” loan with a term of twelve monthes or less
- Reverse mortgage transaction

An escrow account is not required for the following insurance premiums (as described in (b)(2)(ii)):

- For dwellings in condominiums, planned unit developments (PUDs), or other common interest communities in which dwelling ownership requires participation in a governing association and where the governing association maintains a paster policy insuring all dwellings

An escrow account is not required if, at the time of consummation (as described in (b)(2)(iii)):

- A higher-priced mortgage transaction secured by a first lien on a property is located in either a “*rural*” or “*underserved*” area;
- Note the time period:
    - o during the preceding calendar year; or

  - if the application was received before April 1 of the current calendar year, during either of the two preceding calendar years

See (b)(2)(iv)(A) through (C) for description and discussion of "*rural*" and "*underserved*" areas.

The creditor (and its affiliates together) extended no more than 2,000 higher-priced mortgage transactions secured by first liens that were sold, assigned, or otherwise transferred to another person, or were subject at consummation to a commitment to be acquired by another person;

- Note the time period:
  - during the preceding calendar year; or
  - if the application was received before April 1 of the current calendar year, during either of the two preceding calendar years

The creditor (and its affiliates together) that regularly extended higher-priced mortgages secured by first liens had total assets of less than $2 billion (adjusted annually); and

- Note the time period:
  - during the preceding December 31st; or
  - if the application was received before April 1 of the current calendar year, during either of the two preceding December 31sts

Neither the creditor nor its affiliates maintains an escrow account for any extension of consumer credit secured by real property or a dwelling that the creditor (or its affiliate) currently services, except for:

- Escrow accounts established first-lien higher-priced mortgage applications received on or after April 1, 2010 and before May 1, 2016; or
- Escrow accounts established after consummation as an accommodation to distressed consumers to avoid default or foreclosure.

NOTE: An escrow account *must be established*, for any first-lien higher-priced mortgage loan that, at the time of consummation, is subject to a commitment to be acquired by a person that does not satisfy the conditions in (b)(2)(iii), unless otherwise exempted by (b)(2) (as described in (b)(2)(v)).

The commentary provides additional substantial information relative to these exemptions.

Regulatory Text

(b) Escrow accounts

(2) **Exemptions.** Notwithstanding paragraph (b)(1) of this section:

(i) An escrow account need not be established for:

(A) A transaction secured by shares in a cooperative;

(B) A transaction to finance the initial construction of a dwelling;

(C) A temporary or "bridge" loan with a loan term of twelve months or less, such as a loan to purchase a new dwelling where the consumer plans to sell a current dwelling within twelve months; or

(D) A reverse mortgage transaction subject to §1026.33.

(ii) Insurance premiums described in paragraph (b)(1) of this section need not be included in escrow accounts 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.

(iii) Except as provided in paragraph (b)(2)(v) of this section, an escrow account need not be established for a transaction if, at the time of consummation:

(A) During the preceding calendar year, or, if the application for the transaction was received before April 1 of the current calendar year, during either of the two preceding calendar years, the creditor extended a covered transaction, as defined by §1026.43(b)(1), secured by a first lien on a property that is located in an area that is either "rural" or "underserved," as set forth in paragraph (b)(2)(iv) of this section;

(B) During the preceding calendar year, or, if the application for the transaction was received before April 1 of the current calendar year, during either of the two preceding calendar years, the creditor and its affiliates together extended no more than 2,000 covered transactions, as defined by §1026.43(b)(1), secured by first liens, that were sold, assigned, or otherwise transferred to another person, or that were subject at the time of consummation to a commitment to be acquired by another person;

(C) As of the preceding December 31st, or, if the application for the transaction was received before April 1 of the current calendar year, as of either of the two preceding December 31sts, the creditor and its affiliates that regularly extended covered transactions, as defined by §1026.43(b)(1), secured by first liens, together, had total assets of less than $2,000,000,000; this asset threshold shall adjust automatically each year, based on the year-to-year change in the average of the Consumer Price Index for Urban Wage Earners and Clerical Workers, not seasonally adjusted, for each 12-month period ending in November, with rounding to the nearest million dollars (see comment 35(b)(2)(iii)-1.iii for the applicable threshold); and

(D) Neither the creditor nor its affiliate maintains an escrow account of the type described in paragraph (b)(1) of this section for any extension of consumer credit secured by real property or a dwelling that the creditor or its affiliate currently services, other than:

(*1*) Escrow accounts established for first-lien higher-priced mortgage loans for which applications were received on or after April 1, 2010, and before May 1, 2016; or

(*2*) Escrow accounts established after consummation as an accommodation to distressed consumers to assist such consumers in avoiding default or foreclosure.

(iv) For purposes of paragraph (b)(2)(iii)(A) of this section:

(A) An area is "rural" during a calendar year if it is:

(*1*) A county that is neither in a metropolitan statistical area nor in a micropolitan statistical area that is adjacent to a metropolitan statistical area, as those terms are defined by the U.S. Office of Management and Budget and as they are applied under currently applicable Urban Influence Codes (UICs), established by the United States Department of Agriculture's Economic Research Service (USDA-ERS);

(*2*) A census block that is not in an urban area, as defined by the U.S. Census Bureau using the latest decennial census of the United States; or

(*3*) A county or a census block that has been designated as rural by the Bureau pursuant to the application process established under section 89002 of the Helping Expand Lending Practices in Rural Communities Act, Public Law 114-94, title LXXXIX (2015). The provisions of this paragraph (b)(2)(iv)(A)(*3*) shall cease to have any force or effect on December 4, 2017.

(B) An area is "underserved" during a calendar year if, according to Home Mortgage Disclosure Act (HMDA) data for the preceding calendar year, it is a county in which no more than two creditors extended covered transactions, as defined in §1026.43(b)(1), secured by first liens on properties in the county five or more times.

(C) A property shall be deemed to be in an area that is rural or underserved in a particular calendar year if the property is:

(1) Located in a county that appears on the lists published by the Bureau of counties that are rural or underserved, as defined by §1026.35(b)(2)(iv)(A)(1) or §1026.35(b)(2)(iv)(B), for that calendar year,

(2) Designated as rural or underserved for that calendar year by any automated tool that the Bureau provides on its public Web site, or

(3) Not designated as located in an urban area, as defined by the most recent delineation of urban areas announced by the Census Bureau, by any automated address search tool that the U.S. Census Bureau provides on its public Web site for that purpose and that specifically indicates the urban or rural designations of properties.

(v) Notwithstanding paragraph (b)(2)(iii) of this section, an escrow account must be established pursuant to paragraph (b)(1) of this section for any first-lien higher-priced mortgage loan that, at consummation, is subject to a commitment to be acquired by a person that does not satisfy the conditions in paragraph (b)(2)(iii) of this section, unless otherwise exempted by this paragraph (b)(2).

Regulatory Commentary

35(b)(2) Exemptions.

Paragraph 35(b)(2)(i).

*1. **Construction-permanent loans.** Under §1026.35(b)(2)(ii)(B), §1026.35 does not apply to a* *transaction to finance the initial construction of a dwelling. Section 1026.35 may apply, however, to permanent financing that replaces a construction loan, whether the permanent financing is extended by the same or a different creditor. When a construction loan may be permanently financed by the same creditor, §1026.17(c)(6)(ii) permits the creditor to give either one combined disclosure for both the construction financing and the permanent financing, or a separate set of disclosures for each of the two phases as though they were two separate transactions. See also comment 17(c)(6)-2. Section 1026.17(c)(6)(ii) addresses only how a creditor may elect to disclose a construction-permanent transaction. Which disclosure option a creditor elects under §1026.17(c)(6)(ii) does not affect the determination of whether the permanent phase of the transaction is subject to §1026.35. When the creditor discloses the two phases as separate transactions, the annual percentage rate for the permanent phase must be compared to the average prime offer rate for a transaction that is comparable to the permanent financing to determine whether the transaction is a higher-priced mortgage loan under §1026.35(a). When the creditor discloses the two phases as a single transaction, a single annual percentage rate, reflecting the appropriate charges from both phases, must be calculated for the transaction in accordance with §1026.22(a)(1) and appendix D to part 1026. This annual percentage rate must be compared to the average prime offer rate for a transaction that is comparable to the permanent financing to determine the transaction is a higher-priced mortgage loan under §1026.35(a). If the transaction is determined to be a higher-priced mortgage loan, only the permanent phase is subject to the requirement of §1026.35(b)(1) to establish and maintain an escrow account, and the period for which the escrow account must remain in place under §1026.35(b)(3) is measured from the time the conversion to the permanent phase financing occurs.*

Paragraph 35(b)(2)(ii).

1. ***Limited exemption.*** *A creditor is required to escrow for payment of property taxes for all first-lien higher-priced mortgage loans secured by condominium, planned unit development, or similar dwellings or units regardless of whether the creditor escrows for insurance premiums for such dwellings or units.*

2. ***Planned unit developments.*** *Planned unit developments (PUDs) are a form of property ownership often used in retirement communities, golf communities, and similar communities made up of homes located within a defined geographical area. PUDs usually have a homeowners' association or some other governing association, analogous to a condominium association and with similar authority and obligations. Thus, as with condominiums, PUDs often have master insurance policies that cover all units in the PUD. Under §1026.35(b)(2)(ii), if a PUD's governing association is obligated to maintain such a master insurance policy, an escrow account required by §1026.35(b)(1) for a transaction secured by a unit in the PUD need not include escrows for insurance. This exemption applies not only to condominiums and PUDs but also to any other type of property ownership arrangement that has a governing association with an obligation to maintain a master insurance policy.*

3. ***More than one governing association associated with a dwelling.*** *The limited exemption provided pursuant to §1026.35(b)(2)(ii) applies to each master insurance policy for properties with multiple governing associations, to the extent each governing association has an obligation to maintain a master insurance policy.*

Paragraph 35(b)(2)(iii).

1. ***Requirements for exemption.*** *Under §1026.35(b)(2)(iii), except as provided in §1026.35(b)(2)(v), a creditor need not establish an escrow account for taxes and insurance for a higher-priced mortgage loan, provided the following four conditions are satisfied when the higher-priced mortgage loan is consummated:*

   i. *During the preceding calendar year, or during either of the two preceding calendar years if the application for the loan was received before April 1 of the current calendar year, a creditor extended a first-lien covered transaction, as defined in §1026.43(b)(1), secured by a property located in an area that is either "rural" or "underserved," as set forth in §1026.35(b)(2)(iv).*

      A. *In general, whether the rural-or-underserved test is satisfied depends on the creditor's activity during the preceding calendar year. However, if the application for the loan in question was received before April 1 of the current calendar year, the creditor may instead meet the rural-or-underserved test based on its activity during the next-to-last calendar year. This provides creditors with a grace period if their activity meets the rural-or-underserved test (in §1026.35(b)(2)(iii)(A)) in one calendar year but fails to meet it in the next calendar year.*

      B. *A creditor meets the rural-or-underserved test for any higher-priced mortgage loan consummated during a calendar year if it extended a first-lien covered transaction in the preceding calendar year secured by a property located in a rural-or-underserved area. If the creditor does not meet the rural-or-underserved test in the preceding calendar year, the creditor meets this condition for a higher-priced mortgage loan consummated during the current calendar year only if the application for the loan was received before April 1 of the current calendar year and the creditor extended a first-lien covered transaction during the next-to-last calendar year that is secured by a property located in a rural or underserved area. The following examples are illustrative:*

         1. *Assume that a creditor extended during 2016 a first-lien covered transaction that is secured by a property located in a rural or underserved area. Because the creditor extended a first-lien covered transaction during 2016 that is secured by a property located in a rural or underserved area, the creditor can meet this condition for exemption for any higher-priced mortgage loan consummated during 2017.*

         2. *Assume that a creditor did not extend during 2016 a first-lien covered transaction secured by a property that is located in a rural or underserved area. Assume further that the same creditor extended during 2015 a first-lien covered transaction that is located in a rural or underserved area. Assume further that the creditor consummates a higher-priced mortgage loan in 2017 for which the application was received in November 2017. Because the creditor did not extend during 2016 a first-lien covered transaction secured by a property that is located in a rural or underserved area, and the application was received on or after April 1, 2017, the creditor does not meet this condition for exemption. However, assume instead that the creditor consummates a higher-priced mortgage loan in 2017 based on an application received in February 2017. The creditor meets this condition for exemption for this loan because the application was received before April 1, 2017, and the creditor extended during 2015 a first-lien covered transaction that is located in a rural or underserved area.*

   ii. *The creditor and its affiliates together extended no more than 2,000 covered transactions, as* *defined in §1026.43(b)(1), secured by first liens, that were sold, assigned, or otherwise transferred by the creditor or its affiliates to another person, or that were subject at the time of consummation to a commitment to be acquired by another person, during the preceding calendar year or during either of the two preceding calendar years if the application for the loan was received before April 1 of the current calendar year. For purposes of §1026.35(b)(2)(iii)(B), a transfer of a first-lien covered transaction to "another person" includes a transfer by a creditor to its affiliate.*

A. In general, whether this condition is satisfied depends on the creditor's activity during the preceding calendar year. However, if the application for the loan in question is received before April 1 of the current calendar year, the creditor may instead meet this condition based on activity during the next-to-last calendar year. This provides creditors with a grace period if their activity falls at or below the threshold in one calendar year but exceeds it in the next calendar year.

B. For example, assume that in 2015 a creditor and its affiliates together extended 1,500 loans that were sold, assigned, or otherwise transferred by the creditor or its affiliates to another person, or that were subject at the time of consummation to a commitment to be acquired by another person, and 2,500 such loans in 2016. Because the 2016 transaction activity exceeds the threshold but the 2015 transaction activity does not, the creditor satisfies this condition for exemption for a higher-priced mortgage loan consummated during 2017 if the creditor received the application for the loan before April 1, 2017, but does not satisfy this condition for a higher-priced mortgage loan consummated during 2017 if the application for the loan was received on or after April 1, 2017.

C. For purposes of §1026.35(b)(2)(iii)(B), extensions of first-lien covered transactions, during the applicable time period, by all of a creditor's affiliates, as "affiliate" is defined in §1026.32(b)(5), are counted toward the threshold in this section. "Affiliate" is defined in §1026.32(b)(5) as "any company that controls, is controlled by, or is under common control with another company, as set forth in the Bank Holding Company Act of 1956 (12 U.S.C. 1841 et seq.)." Under the Bank Holding Company Act, a company has control over a bank or another company if it "directly or indirectly or acting through one or more persons owns, controls, or has power to vote 25 per centum or more of any class of voting securities of the bank or company"; it "controls in any manner the election of a majority of the directors or trustees of the bank or company"; or the Federal Reserve Board "determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a controlling influence over the management or policies of the bank or company." 12 U.S.C. 1841(a)(2).

iii. As of the end of the preceding calendar year, or as of the end of either of the two preceding calendar years if the application for the loan was received before April 1 of the current calendar year, the creditor and its affiliates that regularly extended covered transactions secured by first liens, together, had total assets that are less than the applicable annual asset threshold.

A. For purposes of §1026.35(b)(2)(iii)(C), in addition to the creditor's assets, only the assets of a creditor's "affiliate" (as defined by §1026.32(b)(5)) that regularly extended covered transactions (as defined by §1026.43(b)(1)) secured by first liens, are counted toward the applicable annual asset threshold. See comment 35(b)(2)(iii)-1.ii.C for discussion of definition of "affiliate."

B. Only the assets of a creditor's affiliate that regularly extended first-lien covered transactions during the applicable period are included in calculating the creditor's assets. The meaning of "regularly extended" is based on the number of times a person extends consumer credit for purposes of the definition of "creditor" in §1026.2(a)(17). Because covered transactions are "transactions secured by a dwelling," consistent with §1026.2(a)(17)(v), an affiliate regularly extended covered transactions if it extended more than five covered transactions in a calendar year. Also consistent with §1026.2(a)(17)(v), because a covered transaction may be a high-cost mortgage subject to §1026.32, an affiliate regularly extends covered transactions if, in any 12-month period, it extends more than one covered transaction that is subject to the requirements of §1026.32 or one or more such transactions through a mortgage broker. Thus, if a creditor's affiliate regularly extended first-lien covered transactions during the preceding calendar year, the creditor's assets as of the end of the preceding calendar year, for purposes of the asset limit, take into account the assets of that affiliate. If the creditor, together with its affiliates that regularly extended first-lien covered transactions, exceeded the asset limit in the preceding calendar year—to be eligible to operate as a small creditor for transactions with applications received before April 1 of the current calendar year—the assets of the creditor's affiliates that regularly extended covered transactions in the year before the preceding calendar year are included in calculating the creditor's assets.

C. If multiple creditors share ownership of a company that regularly extended first-lien covered transactions, the assets of the company count toward the asset limit for a co-owner creditor if the company is an "affiliate," as defined in §1026.32(b)(5), of the co-owner creditor. Assuming the company is not an affiliate of the co-owner creditor by virtue of any other aspect of the definition (such as by the company and co-owner creditor being under common control), the company's assets are included toward the asset limit of the co-owner creditor only if the company is controlled by the co-owner creditor, "as set forth in the Bank Holding Company Act." If the co-owner creditor and the company are affiliates (by virtue of any aspect of the definition), the co-owner creditor counts all of the company's assets toward the asset limit, regardless of the co-owner creditor's ownership share. Further, because the co-owner and the company are mutual affiliates the company also would count all of the co-owner's assets towards its own asset limit. See comment 35(b)(2)(iii)-1.ii.C for discussion of the definition of "affiliate."

D. A creditor satisfies the criterion in §1026.35(b)(2)(iii)(C) for purposes of any higher-priced mortgage loan consummated during 2016, for example, if the creditor (together with its affiliates that regularly extended first-lien covered transactions) had total assets of less than the applicable asset threshold on December 31, 2015. A creditor that (together with its affiliates that regularly extended first-lien covered transactions) did not meet the applicable asset threshold on December 31, 2015 satisfies this criterion for a higher-priced mortgage loan consummated during 2016 if the application for the loan was received before April 1, 2016 and the creditor (together with its affiliates that regularly extended first-lien covered transactions) had total assets of less than the applicable asset threshold on December 31, 2014.

E. Under §1026.35(b)(2)(iii)(C), the $2,000,000,000 asset threshold adjusts automatically each year based on the year-to-year change in the average of the Consumer Price Index for Urban Wage Earners and Clerical Workers, not seasonally adjusted, for each 12-month period ending in November, with rounding to the nearest million dollars. The

Bureau will publish notice of the asset threshold each year by amending this comment. For calendar year 2016, the asset threshold is $2,052,000,000. A creditor that together with the assets of its affiliates that regularly extended first-lien covered transactions during calendar year 2015 has total assets of less than $2,052,000,000 on December 31, 2015, satisfies this criterion for purposes of any loan consummated in 2016 and for purposes of any loan consummated in 2017 for which the application was received before April 1, 2017. For historical purposes:

1. *For calendar year 2013, the asset threshold was $2,000,000,000. Creditors that had total assets of less than $2,000,000,000 on December 31, 2012, satisfied this criterion for purposes of the exemption during 2013.*
2. *For calendar year 2014, the asset threshold was $2,028,000,000. Creditors that had total assets of less than $2,028,000,000 on December 31, 2013, satisfied this criterion for purposes of the exemption during 2014.*
3. *For calendar year 2015, the asset threshold was $2,060,000,000. Creditors that had total assets of less than $2,060,000,000 on December 31, 2014, satisfied this criterion for purposes of any loan consummated in 2015 and, if the creditor's assets together with the assets of its affiliates that regularly extended first-lien covered transactions during calendar year 2014 were less than that amount, for purposes of any loan consummated in 2016 for which the application was received before April 1, 2016.*

iv. The creditor and its affiliates do not maintain an escrow account for any mortgage transaction being serviced by the creditor or its affiliate at the time the transaction is consummated, except as provided in §1026.35(b)(2)(iii)(D)(1) and (2). Thus, the exemption applies, provided the other conditions of §1026.35(b)(2)(iii) are satisfied, even if the creditor previously maintained escrow accounts for mortgage loans, provided it no longer maintains any such accounts except as provided in §1026.35(b)(2)(iii)(D)(1) and (2). Once a creditor or its affiliate begins escrowing for loans currently serviced other than those addressed in §1026.35(b)(2)(iii)(D)(1) and (2), however, the creditor and its affiliate become ineligible for the exemption in §1026.35(b)(2)(iii) on higher-priced mortgage loans they make while such escrowing continues. Thus, as long as a creditor (or its affiliate) services and maintains escrow accounts for any mortgage loans, other than as provided in §1026.35(b)(2)(iii)(D)(1) and (2), the creditor will not be eligible for the exemption for any higher-priced mortgage loan it may make. For purposes of §1026.35(b)(2)(iii), a creditor or its affiliate "maintains" an escrow account only if it services a mortgage loan for which an escrow account has been established at least through the due date of the second periodic payment under the terms of the legal obligation.

Paragraph 35(b)(2)(iii)(D)(1).

1. ***Exception for certain accounts.*** *Escrow accounts established for first-lien higher-priced mortgage loans for which applications were received on or after April 1, 2010, and before May 1, 2016, are not counted for purposes of §1026.35(b)(2)(iii)(D). For applications received on and after May 1, 2016, creditors, together with their affiliates, that establish new escrow accounts, other than those described in §1026.35(b)(2)(iii)(D)(2), do not qualify for the exemption provided under §1026.35(b)(2)(iii). Creditors, together with their affiliates, that continue to maintain escrow accounts established for first-lien higher-priced mortgage loans for which applications were received on or after April 1, 2010, and before May 1, 2016, still qualify for the exemption*

provided under §1026.35(b)(2)(iii) so long as they do not establish new escrow accounts for transactions for which they received applications on or after May 1, 2016, other than those described in §1026.35(b)(2)(iii)(D)(2), and they otherwise qualify under §1026.35(b)(2)(iii).

Paragraph 35(b)(2)(iii)(D)(2).

*1. **Exception for post-consummation escrow accounts for distressed consumers.** An escrow account established after consummation for a distressed consumer does not count for purposes of §1026.35(b)(2)(iii)(D). Distressed consumers are consumers who are working with the creditor or servicer to attempt to bring the loan into a current status through a modification, deferral, or other accommodation to the consumer. A creditor, together with its affiliates, that establishes escrow accounts after consummation as a regular business practice, regardless of whether consumers are in distress, does not qualify for the exception described in §1026.35(b)(2)(iii)(D)(2).*

Paragraph 35(b)(2)(iv).

*1. **Requirements for "rural" or "underserved" status.** An area is considered to be "rural" or "underserved" during a calendar year for purposes of §1026.35(b)(2)(iii)(A) if it satisfies either the definition for "rural" or the definition for "underserved" in §1026.35(b)(2)(iv). A creditor's extensions of covered transactions, as defined by §1026.43(b)(1), secured by first liens on properties located in such areas are considered in determining whether the creditor satisfies the condition in §1026.35(b)(2)(iii)(A). See comment 35(b)(2)(iii)-1.*

i. Under §1026.35(b)(2)(iv)(A), an area is rural during a calendar year if it is: A county that is neither in a metropolitan statistical area nor in a micropolitan statistical area that is adjacent to a metropolitan statistical area; a census block that is not in an urban area, as defined by the U.S. Census Bureau using the latest decennial census of the United States; or a county or a census block that has been designated as "rural" by the Bureau pursuant to the application process established in 2016. See Application Process for Designation of Rural Area under Federal Consumer Financial Law; Procedural Rule, 81 FR 11099 (Mar. 3, 2016). Metropolitan statistical areas and micropolitan statistical areas are defined by the Office of Management and Budget and applied under currently applicable Urban Influence Codes (UICs), established by the United States Department of Agriculture's Economic Research Service (USDA-ERS). For purposes of §1026.35(b)(2)(iv)(A)(1), "adjacent" has the meaning applied by the USDA-ERS in determining a county's UIC; as so applied, "adjacent" entails a county not only being physically contiguous with a metropolitan statistical area but also meeting certain minimum population commuting patterns. A county is a "rural" area under §1026.35(b)(2)(iv)(A)(1) if the USDA-ERS categorizes the county under UIC 4, 6, 7, 8, 9, 10, 11, or 12. Descriptions of UICs are available on the USDA-ERS Web site at http://www.ers.usda.gov/data-products/urban-influence-codes/documentation.aspx. A county for which there is no currently applicable UIC (because the county has been created since the USDA-ERS last categorized counties) is a rural area only if all counties from which the new county's land was taken are themselves rural under currently applicable UICs.

ii. Under §1026.35(b)(2)(iv)(B), an area is underserved during a calendar year if, according to Home Mortgage Disclosure Act (HMDA) data for the preceding calendar year, it is a county in which no more than two creditors extended covered transactions, as defined in

§1026.43(b)(1), secured by first liens, five or more times on properties in the county. Specifically, a county is an "underserved" area if, in the applicable calendar year's public HMDA aggregate dataset, no more than two creditors have reported five or more first-lien covered transactions, with HMDA geocoding that places the properties in that county. For purposes of this determination, because only covered transactions are counted, all first-lien originations (and only first-lien originations) reported in the HMDA data are counted except those for which the owner-occupancy status is reported as "Not owner-occupied" (HMDA code 2), the property type is reported as "Multifamily" (HMDA code 3), the applicant's or co-applicant's race is reported as "Not applicable" (HMDA code 7), or the applicant's or co-applicant's sex is reported as "Not applicable" (HMDA code 4). The most recent HMDA data are available at http://www.ffiec.gov/hmda.

iii.

A. Each calendar year, the Bureau applies the "underserved" area test and the "rural" area test to each county in the United States. If a county satisfies either test, the Bureau will include the county on a published list of counties that are rural or underserved as defined by §1026.35(b)(2)(iv)(A)(1) or §1026.35(b)(2)(iv)(B) for a particular calendar year, even if the county contains census blocks that are designated by the Census Bureau as urban. To facilitate compliance with appraisal requirements in §1026.35(c), the Bureau also creates a list of those counties that are rural under the Bureau's definition without regard to whether the counties are underserved. To the extent that U.S. territories are treated by the Census Bureau as counties and are neither metropolitan statistical areas nor micropolitan statistical areas adjacent to metropolitan statistical areas, such territories will be included on these lists as rural areas in their entireties. The Bureau will post on its public Web site the applicable lists for each calendar year by the end of that year and publish such lists in the FEDERAL REGISTER, to assist creditors in ascertaining the availability to them of the exemption during the following year. Any county that the Bureau includes on its published lists of counties that are rural or underserved under the Bureau's definitions for a particular year is deemed to qualify as a rural or underserved area for that calendar year for purposes of §1026.35(b)(2)(iv), even if the county contains census blocks that are designated by the Census Bureau as urban. A property located in such a listed county is deemed to be located in a rural or underserved area, even if the census block in which the property is located is designated as urban.

B. A property is deemed to be in a rural or underserved area according to the definitions in §1026.35(b)(2)(iv) during a particular calendar year if it is identified as such by an automated tool provided on the Bureau's public Web site. A printout or electronic copy from the automated tool provided on the Bureau's public Web site designating a particular property as being in a rural or underserved area may be used as "evidence of compliance" that a property is in a rural or underserved area, as defined in §1026.35(b)(2)(iv)(A) and (B), for purposes of the record retention requirements in §1026.25.

C. The U.S. Census Bureau may provide on its public Web site an automated address search tool that specifically indicates if a property is located in an urban area for purposes of the Census Bureau's most recent delineation of urban areas. For any calendar year that began after the date on which the Census Bureau announced its most recent delineation of urban areas, a property is deemed to be in a rural area if the search results provided for the property by any such automated address search tool available on the Census Bureau's public Web site do not designate the property as being in an urban area. A *printout or electronic copy from such an automated address search tool available on the Census Bureau's public Web site designating a particular property as not being in an urban area may be used as "evidence of compliance" that the property is in a rural area, as defined in §1026.35(b)(2)(iv)(A), for purposes of the record retention requirements in §1026.25.*

D. For a given calendar year, a property qualifies for a safe harbor if any of the enumerated safe harbors affirms that the property is in a rural or underserved area or not in an urban area. For example, the Census Bureau's automated address search tool may indicate a property is in an urban area, but the Bureau's rural or underserved counties list indicates the property is in a rural or underserved county. The property in this example is in a rural or underserved area because it qualifies under the safe harbor for the rural or underserved counties list. The lists of counties published by the Bureau, the automated tool on its public Web site, and the automated address search tool available on the Census Bureau's public Web site, are not the exclusive means by which a creditor can demonstrate that a property is in a rural or underserved area as defined in §1026.35(b)(2)(iv)(A) and (B). However, creditors are required to retain "evidence of compliance" in accordance with §1026.25, including determinations of whether a property is in a rural or underserved area as defined in §1026.35(b)(2)(iv)(A) and (B).

*2. **Examples.***

i. An area is considered "rural" for a given calendar year based on the most recent available UIC designations by the USDA-ERS and the most recent available delineations of urban areas by the U.S. Census Bureau that are available at the beginning of the calendar year. These designations and delineations are updated by the USDA-ERS and the U.S. Census Bureau respectively once every ten years. As an example, assume a creditor makes first-lien covered transactions in Census Block X that is located in County Y during calendar year 2017. As of January 1, 2017, the most recent UIC designations were published in the second quarter of 2013, and the most recent delineation of urban areas was announced in the FEDERAL REGISTER in 2012, see U.S. Census Bureau, Qualifying Urban Areas for the 2010 Census, 77 FR 18652 (Mar. 27, 2012). To determine whether County Y is rural under the Bureau's definition during calendar year 2017, the creditor can use USDA-ERS's 2013 UIC designations. If County Y is not rural, the creditor can use the U.S. Census Bureau's 2012 delineation of urban areas to determine whether Census Block X is rural and is therefore a "rural" area for purposes of §1026.35(b)(2)(iv)(A). In addition, an area is considered "rural" if it is a county or a census block that has been designated as rural by the Bureau using the application process established in 2016. See Application Process for Designation of Rural Area under Federal Consumer Financial Law; Procedural Rule, 81 FR 11099 (Mar. 3, 2016). Designations under this process are time-limited and expire on December 4, 2017.

ii. A county is considered an "underserved" area for a given calendar year based on the most recent available HMDA data. For example, assume a creditor makes first-lien covered transactions in County Y during calendar year 2016, and the most recent HMDA data are for calendar year 2015, published in the third quarter of 2016. The creditor will use the 2015 HMDA data to determine "underserved" area status for County Y in calendar year 2016 for the purposes of qualifying for the "rural or underserved" exemption for any higher-priced mortgage loans consummated in calendar year 2017 or for any higher-priced mortgage loan consummated during 2018 for which the application was received before April 1, 2018.

Paragraph 35(b)(2)(v).

1. ***Forward commitments.*** *A creditor may make a mortgage loan that will be transferred or sold to a purchaser pursuant to an agreement that has been entered into at or before the time the loan is consummated. Such an agreement is sometimes known as a "forward commitment." Even if a creditor is otherwise eligible for the exemption in §1026.35(b)(2)(iii), a first-lien higher-priced mortgage loan that will be acquired by a purchaser pursuant to a forward commitment is subject to the requirement to establish an escrow account under §1026.35(b)(1) unless the purchaser is also eligible for the exemption in §1026.35(b)(2)(iii) or the transaction is otherwise exempt under §1026.35(b)(2). The escrow requirement applies to any such transaction, whether the forward commitment provides for the purchase and sale of the specific transaction or for the purchase and sale of mortgage obligations with certain prescribed criteria that the transaction meets. For example, assume a creditor that qualifies for the exemption in §1026.35(b)(2)(iii) makes a higher-priced mortgage loan that meets the purchase criteria of an investor with which the creditor has an agreement to sell such mortgage obligations after consummation. If the investor is ineligible for the exemption in §1026.35(b)(2)(iii), an escrow account must be established for the transaction before consummation in accordance with §1026.35(b)(1) unless the transaction is otherwise exempt (such as a reverse mortgage or home equity line of credit).*

Escrow Accounts - Cancellation - 12 CFR § 1026.35(b)(3)

Regulatory Discussion

The section describes the conditions which must be satisfied in order for the creditor to cancel an escrow account. Generally, an escrow account may be cancelled upon the earlier of:

- Termination of the debt; or
- Receipt of a consumer's request to cancel (no earlier than five years after consummation of the debt).

Except: an escrow account shall not be cancelled pursuant to a consumer's request unless:

- The unpaid principal balance is less than 80% of the "*original value*" (see commentary for definition) of the property securing the debt; and
- The consumer currently is not delinquent or in default on the debt.

Regulatory Text

(b) Escrow accounts

(3) **Cancellation**

(i) **General.** Except as provided in paragraph (b)(3)(ii) of this section, a creditor or servicer may cancel an escrow account required in paragraph (b)(1) of this section only upon the earlier of:

(A) Termination of the underlying debt obligation; or

(B) Receipt no earlier than five years after consummation of a consumer's request to cancel the escrow account.

(ii) **Delayed cancellation.** Notwithstanding paragraph (b)(3)(i) of this section, a creditor or servicer shall not cancel an escrow account pursuant to a consumer's request described in paragraph (b)(3)(i)(B) of this section unless the following conditions are satisfied:

(A) The unpaid principal balance is less than 80 percent of the original value of the property securing the underlying debt obligation; and

(B) The consumer currently is not delinquent or in default on the underlying debt obligation.

Regulatory Commentary

35(b)(3) Cancellation.

1. ***Termination of underlying debt obligation.*** *Section 1026.35(b)(3)(i) provides that, in general, an escrow account required by §1026.35(b)(1) may not be cancelled until the underlying debt obligation is terminated or the consumer requests cancellation at least five years after consummation. Methods by which an underlying debt obligation may be terminated include, among other things, repayment, refinancing, rescission, and foreclosure.*

2. ***Minimum durations***. *Section 1026.35(b)(3) establishes minimum durations for which escrow accounts established pursuant to §1026.35(b)(1) must be maintained. This requirement does not affect a creditor's right or obligation, pursuant to the terms of the legal obligation or applicable law, to offer or require an escrow account thereafter.*

3. ***Less than eighty percent unpaid principal balance***. *The term "original value" in §1026.35(b)(3)(ii)(A) means the lesser of the sales price reflected in the sales contract for the property, if any, or the appraised value of the property at the time the transaction was consummated. In determining whether the unpaid principal balance has reached less than 80 percent of the original value of the property securing the underlying debt, the creditor or servicer shall count any subordinate lien of which it has reason to know. If the consumer certifies in writing that the equity in the property securing the underlying debt obligation is unencumbered by a subordinate lien, the creditor or servicer may rely upon the certification in making its determination unless it has actual knowledge to the contrary.*

Section 3: Appraisals
12 C.F.R. § 1026.35(c)

Appraisals - Definitions - 12 CFR § 1026.35(c)(1)

Regulatory Discussion

This section defines seven specific terms associated with appraisals with respect to higher-priced mortgage transactions.

Regulatory Text

(c) Appraisals.

(1) **Definitions.** For purposes of this section:

(i) **Certified or licensed appraiser** means a person who is certified or licensed by the State agency in the State in which the property that secures the transaction is located, and who performs the appraisal in conformity with the Uniform Standards of Professional Appraisal Practice and the requirements applicable to appraisers in title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (12 U.S.C. 3331 *et seq.*), and any implementing regulations in effect at the time the appraiser signs the appraiser's certification.

(ii) **Credit risk** means the financial risk that a consumer will default on a loan.

(iii) **Manufactured home** has the same meaning as in 24 CFR 3280.2.

(iv) **Manufacturer's invoice** means a document issued by a manufacturer and provided with a manufactured home to a retail dealer that separately details the wholesale (base) prices at the factory for specific models or series of manufactured homes and itemized options (large appliances, built-in items and equipment), plus actual itemized charges for freight from the factory to the dealer's lot or the homesite (including any rental of wheels and axles) and for any sales taxes to be paid by the dealer. The invoice may recite such prices and charges on an itemized basis or by stating an aggregate price or charge, as appropriate, for each category.

(v) **National Registry** means the database of information about State certified and licensed appraisers maintained by the Appraisal Subcommittee of the Federal Financial Institutions Examination Council.

(vi) **New manufactured home** means a manufactured home that has not been previously occupied.

(vii) **State agency** means a “State appraiser certifying and licensing agency” recognized in accordance with section 1118(b) of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (12 U.S.C. 3347(b)) and any implementing regulations.

Regulatory Commentary

35(c)(1)(i) Certified or Licensed Appraiser

1. ***USPAP.*** *The Uniform Standards of Professional Appraisal Practice (USPAP) are established by the Appraisal Standards Board of the Appraisal Foundation (as defined in 12 U.S.C. 3350(9)). Under §1026.35(c)(1)(i), the relevant USPAP standards are those found in the edition of USPAP and that are in effect at the time the appraiser signs the appraiser's certification.*

2. ***Appraiser's certification.*** *The appraiser's certification refers to the certification that must be signed by the appraiser for each appraisal assignment. This requirement is specified in USPAP Standards Rule 2-3.*

3. ***FIRREA title XI and implementing regulations.*** *The relevant regulations are those prescribed under section 1110 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), as amended (12 U.S.C. 3339), that relate to an appraiser's development and reporting of the appraisal in effect at the time the appraiser signs the appraiser's certification. Paragraph (3) of FIRREA section 1110 (12 U.S.C. 3339(3)), which relates to the review of appraisals, is not relevant for determining whether an appraiser is a certified or licensed appraiser under §1026.35(c)(1)(i).*

Appraisals - Exemptions - 12 CFR § 1026.35(c)(2)

Regulatory Discussion

This section describes eight specific transactions that are exempt from the appraisal requirements for higher-priced mortgage transactions.

The exemptions in items (i) through (vi) are relatively straightforward; the exemptions in items (vii) and (viii) are more complex.

The commentary provides important additional information for the exemptions in items (i), (ii), (iii), (iv), (vii), and (viii).

Regulatory Text

(c) Appraisals.

(2) **Exemptions.** Unless otherwise specified, the requirements in paragraph (c)(3) through (6) of this section do not apply to the following types of transactions:

(i) A loan that satisfies the criteria of a qualified mortgage as defined pursuant to 15 U.S.C. 1639c;

(ii) An extension of credit for which the amount of credit extended is equal to or less than the applicable threshold amount, which is adjusted every year to reflect increases in the Consumer Price Index for Urban Wage Earners and Clerical Workers, as applicable, and published in the official staff commentary to this paragraph (c)(2)(ii);

(iii) A transaction secured by a mobile home, boat, or trailer.

(iv) A transaction to finance the initial construction of a dwelling.

(v) A loan with a maturity of 12 months or less, if the purpose of the loan is a "bridge" loan connected with the acquisition of a dwelling intended to become the consumer's principal dwelling.

(vi) A reverse-mortgage transaction subject to 12 CFR 1026.33(a).

(vii) An extension of credit that is a refinancing secured by a first lien, with refinancing defined as in §1026.20(a) (except that the creditor need not be the original creditor or a holder or servicer of the original obligation), provided that the refinancing meets the following criteria:

(A) Either

(1) The credit risk of the refinancing is retained by the person that held the credit risk of the existing obligation and there is no commitment, at consummation, to transfer the credit risk to another person; or

(2) The refinancing is insured or guaranteed by the same Federal government agency that insured or guaranteed the existing obligation;

(B) The regular periodic payments under the refinance loan do not

(1) Cause the principal balance to increase;

(2) Allow the consumer to defer repayment of principal; or

(3) Result in a balloon payment, as defined in §1026.18(s)(5)(i); and

(C) The proceeds from the refinancing are used solely to satisfy the existing obligation and amounts attributed solely to the costs of the refinancing; and

(viii) A transaction secured by:

(A) A new manufactured home and land, but the exemption shall only apply to the requirement in paragraph (c)(3)(i) of this section that the appraiser conduct a physical visit of the interior of the new manufactured home; or

(B) A manufactured home and not land, for which the creditor obtains one of the following and provides a copy to the consumer no later than three business days prior to consummation of the transaction—

(1) For a new manufactured home, the manufacturer's invoice for the manufactured home securing the transaction, provided that the date of manufacture is no earlier than 18 months prior to the creditor's receipt of the consumer's application for credit;

(2) A cost estimate of the value of the manufactured home securing the transaction obtained from an independent cost service provider; or

(3) A valuation, as defined in §1026.42(b)(3), of the manufactured home performed by a person who has no direct or indirect interest, financial or otherwise, in the property or transaction for which the valuation is performed and has training in valuing manufactured homes.

Regulatory Commentary

35(c)(2) Exemptions

1. ***Compliance with title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA).*** *Section 1026.35(c)(2) provides exemptions solely from the requirements of section 1026.35(c)(3) through (6). Institutions subject to the requirements of FIRREA and its implementing regulations that make a loan qualifying for an exemption under section 1026.35(c)(2) must still comply with appraisal and evaluation requirements under FIRREA and its implementing regulations.*

Paragraph 35(c)(2)(i)

1. ***Qualified mortgage criteria.*** *Under §1026.35(c)(2)(i), a loan is exempt from the appraisal requirements of §1026.35(c) if either:*

   i. The loan is

   (1) subject to the Bureau's ability-to-repay requirements in §1026.43 as a "covered transaction" (defined in §1026.43(b)(1)) and (2) a qualified mortgage pursuant to the Bureau's rules or, for loans insured, guaranteed, or administered by the U.S. Department of Housing and Urban Development (HUD), U.S. Department of Veterans Affairs (VA), U.S. Department of Agriculture (USDA), or Rural Housing Service (RHS), a qualified mortgage pursuant to applicable rules prescribed by those agencies (but only once such rules are in effect; otherwise, the Bureau's definition of a qualified mortgage applies to those loans); or

   ii. The loan is

   (1) not subject to the Bureau's ability-to-repay requirements in §1026.43 as a "covered transaction" (defined in §1026.43(b)(1)), but (2) meets the criteria for a qualified mortgage in the Bureau's rules or, for loans insured, guaranteed, or administered by HUD, VA, USDA, or RHS, meets the criteria for a qualified mortgage in the applicable rules prescribed by those agencies (but only once such rules are in effect; otherwise, the Bureau's criteria for a qualified mortgage applies to those loans). To explain further, loans enumerated in §1026.43(a) are not "covered transactions" under the Bureau's ability-to-repay requirements in §1026.43, and thus cannot be qualified mortgages (entitled to a rebuttable presumption or safe harbor of compliance with the ability-to-repay requirements of §1026.43, see, e.g., §1026.43(e)(1)). These include an extension of credit made pursuant to a program administered by a Housing Finance Agency, as defined under 24 CFR 266.5, or pursuant to a program authorized by sections 101 and 109 of the Emergency Economic Stabilization Act of 2008. See §1026.43(a)(3)(iv) and

(vi). They also include extensions of credit made by a creditor identified in §1026.43(a)(3)(v). However, these loans are eligible for the exemption in §1026.35(c)(2)(i) if they meet the Bureau's qualified mortgage criteria in §1026.43(e)(2), (4), (5), or (6) or §1026.43(f) (including limits on when loans must be consummated) or, for loans that are insured, guaranteed, or administered by HUD, VA, USDA, or RHS, in applicable rules prescribed by those agencies (but only once such rules are in effect; otherwise, the Bureau's criteria for a qualified mortgage applies to those loans). For example, assume that HUD has prescribed rules to define loans insured under its programs that are qualified mortgages and those rules are in effect. Assume further that a creditor designated as a Community Development Financial Institution, as defined under 12 CFR 1805.104(h), originates a loan insured by the Federal Housing Administration, which is a part of HUD. The loan is not a "covered transaction" and thus is not a qualified mortgage. See §1026.43(a)(3)(v)(A) and (b)(1). Nonetheless, the transaction is eligible for an exemption from the appraisal requirements of §1026.35(c) if it meets the qualified mortgage criteria in HUD's rules. Nothing in §1026.35(c)(2)(i) alters the definition of a qualified mortgage under regulations of the Bureau, HUD, VA, USDA, or RHS.

Paragraph 35(c)(2)(ii)

1. ***Threshold amount.*** *For purposes of §1026.35(c)(2)(ii), the threshold amount in effect during a particular one-year period is the amount stated below for that period. The threshold amount is adjusted effective January 1 of every year by the percentage increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) that was in effect on the preceding June 1. Every year, this comment will be amended to provide the threshold amount for the upcoming one-year period after the annual percentage change in the CPI-W that was in effect on June 1 becomes available. Any increase in the threshold amount will be rounded to the nearest $100 increment. For example, if the percentage increase in the CPI-W would result in a $950 increase in the threshold amount, the threshold amount will be increased by $1,000. However, if the percentage increase in the CPI-W would result in a $949 increase in the threshold amount, the threshold amount will be increased by $900.*

   i. through iv. Omitted.

   v. From January 1, 2019, through December 31, 2019, the threshold amount is $26,700.

2. ***Qualifying for exemption - in general.*** *A transaction is exempt under §1026.35(c)(2)(ii) if the creditor makes an extension of credit at consummation that is equal to or below the threshold amount in effect at the time of consummation.*

3. ***Qualifying for exemption - subsequent changes.*** *A transaction does not meet the condition for an exemption under §1026.35(c)(2)(ii) merely because it is used to satisfy and replace an existing exempt loan, unless the amount of the new extension of credit is equal to or less than the applicable threshold amount. For example, assume a closed-end loan that qualified for a §1026.35(c)(2)(ii) exemption at consummation in year one is refinanced in year ten and that the new loan amount is greater than the threshold amount in effect in year ten. In these circumstances, the creditor must comply with all of the applicable requirements of §1026.35(c) with respect to the year ten transaction if the original loan is satisfied and replaced by the new loan, unless another exemption from the requirements of §1026.35(c) applies. See §1026.35(c)(2) and §1026.35(c)(4)(vii).*

Paragraph 35(c)(2)(iii)

1. ***Secured by a mobile home.*** *For purposes of the exemption in §1026.35(c)(2)(iii), a mobile home does not include a manufactured home, as defined in §1026.35(c)(1)(ii).*

Paragraph 35(c)(2)(iv)

1. ***Construction-to-permanent loans.*** *Section 1026.35(c) does not apply to a transaction to finance the initial construction of a dwelling. This exclusion applies to a construction-only loan as well as to the construction phase of a construction-to-permanent loan. Section 1026.35(c) does apply, however, to permanent financing that replaces a construction loan, whether the permanent financing is extended by the same or a different creditor, unless the permanent financing is otherwise exempt from the requirements of §1026.35(c). See §1026.35(c)(2). When a construction loan may be permanently financed by the same creditor, the general disclosure requirements for closed-end credit (§1026.17) provide that the creditor may give either one combined disclosure for both the construction financing and the permanent financing, or a separate set of disclosures for each of the two phases as though they were two separate transactions. See §1026.17(c)(6)(ii) and comment 17(c)(6)-2. Section 1026.17(c)(6)(ii) addresses only how a creditor may elect to disclose a construction-to-permanent transaction. Which disclosure option a creditor elects under §1026.17(c)(6)(ii) does not affect the determination of whether the permanent phase of the transaction is subject to §1026.35(c). When the creditor discloses the two phases as separate transactions, the annual percentage rate for the permanent phase must be compared to the average prime offer rate for a transaction that is comparable to the permanent financing to determine coverage under §1026.35(c). When the creditor discloses the two phases as a single transaction, a single annual percentage rate, reflecting the appropriate charges from both phases, must be calculated for the transaction in accordance with §1026.35 and appendix D to part 1026. The annual percentage rate must be compared to the average prime offer rate for a transaction that is comparable to the permanent financing to determine coverage under §1026.35(c). If the transaction is determined to be a higher-priced mortgage loan not otherwise exempt under §1026.35(c)(2), only the permanent phase is subject to the requirements of §1026.35(c).*

2. ***Financing initial construction**. The exemption for construction loans in §1026.35(c)(2)(iv) applies to temporary financing of the construction of a dwelling that will be replaced by permanent financing once construction is complete. The exemption does not apply, for example, to loans to finance the purchase of manufactured homes that have not been or are in the process of being built when the financing obtained by the consumer at that time is permanent. See §1026.35(c)(2)(viii).*

Paragraph 35(c)(2)(vii)(A)(1)

1. ***Same credit risk holder.*** *The requirement that the holder of the credit risk on the existing obligation and the refinancing be the same applies to situations in which an entity bears the financial responsibility for the default of a loan by either holding the loan in its portfolio or guaranteeing payments of principal and any interest to investors in a mortgage-backed security in which the loan is pooled. See §1026.35(c)(1)(ii) (defining "credit risk"). For example, a credit risk holder could be a bank that bears the credit risk on the existing obligation by holding the loan in the bank's portfolio. Another example of a credit risk holder would be a government-sponsored enterprise that bears the risk of default on a loan by guaranteeing the payment of principal and any interest on a loan to investors in a mortgage-backed security. The holder of*

credit risk under §1026.35(c)(2)(vii)(A)(1) does not mean individual investors in a mortgage-backed security or providers of private mortgage insurance.

2. ***Same credit risk holder - illustrations***. *Illustrations of the credit risk holder of the existing obligation continuing to be the credit risk holder of the refinancing include, but are not limited to, the following:*

   i. *The existing obligation is held in the portfolio of a bank, thus the bank holds the credit risk. The bank arranges to refinance the loan and also will hold the refinancing in its portfolio. If the refinancing otherwise meets the requirements for an exemption under §1026.35(c)(2)(vii), the transaction will qualify for the exemption because the credit risk holder is the same for the existing obligation and the refinance transaction. In this case, the exemption would apply regardless of whether the bank arranged to refinance the loan directly or indirectly, such as through the servicer or subservicer on the existing obligation.*

   ii. *The existing obligation is held in the portfolio of a government-sponsored enterprise (GSE), thus the GSE holds the credit risk. The existing obligation is then refinanced by the servicer of the loan and immediately transferred to the GSE. The GSE pools the refinancing in a mortgage-backed security guaranteed by the GSE, thus the GSE holds the credit risk on the refinance loan. If the refinance transaction otherwise meets the requirements for an exemption under §1026.35(c)(2)(vii), the transaction will qualify for the exemption because the credit risk holder is the same for the existing obligation and the refinance transaction. In this case, the exemption would apply regardless of whether the existing obligation was refinanced by the servicer or subservicer on the existing obligation (acting as a "creditor" under §1026.2(a)(17)) or by a different creditor.*

3. ***Forward commitments.*** *A creditor may make a mortgage loan that will be sold or otherwise transferred pursuant to an agreement that has been entered into at or before the time the transaction is consummated. Such an agreement is sometimes known as a "forward commitment." A refinance loan does not satisfy the requirement of §1026.35(c)(2)(vii)(A)(1) if the loan will be acquired pursuant to a forward commitment, such that the credit risk on the refinance loan will transfer to a person who did not hold the credit risk on the existing obligation.*

Paragraph 35(c)(2)(vii)(B)

1. ***Regular periodic payments.*** *Under §1026.35(c)(2)(vii)(B), the regular periodic payments on the refinance loan must not: result in an increase of the principal balance (negative amortization); allow the consumer to defer repayment of principal (see comment 43(e)(2)(i)-2); or result in a balloon payment. Thus, the terms of the legal obligation must require the consumer to make payments of principal and interest on a monthly or other periodic basis that will repay the loan amount over the loan term. Except for payments resulting from any interest rate changes after consummation in an adjustable-rate or step-rate mortgage, the periodic payments must be substantially equal. For an explanation of the term "substantially equal," see comment 43(c)(5)(i)-4. In addition, a single-payment transaction is not a refinancing meeting the requirements of §1026.35(c)(2)(vii) because it does not require "regular periodic payments."*

Paragraph 35(c)(2)(vii)(C)

1. ***Permissible use of proceeds.*** *The exemption for a refinancing under §1026.35(c)(2)(vii) is*

available only if the proceeds from the refinancing are used exclusively for the existing obligation and amounts attributed solely to the costs of the refinancing. The existing obligation includes the unpaid principal balance of the existing first lien loan, any earned unpaid finance charges, and any other lawful charges related to the existing loan. For guidance on the meaning of refinancing costs, see comment 23(f)-4. If the proceeds of a refinancing are used for other purposes, such as to pay off other liens or to provide additional cash to the consumer for discretionary spending, the transaction does not qualify for the exemption for a refinancing under §1026.35(c)(2)(vii) from the appraisal requirements in §1026.35(c)

Paragraph 35(c)(2)(viii)(A)

1. ***Secured by new manufactured home and land - physical visit of the interior.*** *A transaction secured by a new manufactured home and land is subject to the requirements of §1026.35(c)(3) through (6) except for the requirement in §1026.35(c)(3)(i) that the appraiser conduct a physical inspection of the interior of the property. Thus, for example, a creditor of a loan secured by a new manufactured home and land could comply with §1026.35(c)(3)(i) by obtaining an appraisal conducted by a state-certified or -licensed appraiser based on plans and specifications for the new manufactured home and an inspection of the land on which the property will be sited, as well as any other information necessary for the appraiser to complete the appraisal assignment in conformity with the Uniform Standards of Professional Appraisal Practice and the requirements of FIRREA and any implementing regulations.*

Paragraph 35(c)(2)(viii)(B)

1. ***Secured by a manufactured home and not land.*** *Section 1026.35(c)(2)(viii)(B) applies to a higher-priced mortgage loan secured by a manufactured home and not land, regardless of whether the home is titled as realty by operation of state law.*

Paragraph 35(c)(2)(viii)(B)(2)

1. ***Independent.*** *A cost service provider from which the creditor obtains a manufactured home unit cost estimate under §1026.35(c)(2)(viii)(B)(2) is "independent" if that person is not affiliated with the creditor in the transaction, such as by common corporate ownership, and receives no direct or indirect financial benefits based on whether the transaction is consummated.*

2. ***Adjustments.*** *The requirement that the cost estimate be from an independent cost service provider does not prohibit a creditor from providing a cost estimate that reflects adjustments to account for factors such as special features, condition or location. However, the requirement that the estimate be obtained from an independent cost service provider means that any adjustments to the estimate must be based on adjustment factors available as part of the independent cost service used, with associated values that are determined by the independent cost service.*

Paragraph 35(c)(2)(viii)(C)(3)

1. ***Interest in the property.*** *A person has a direct or indirect in the property if, for example, the person has any ownership or reasonably foreseeable ownership interest in the manufactured*

home. To illustrate, a person who seeks a loan to purchase the manufactured home to be valued has a reasonably foreseeable ownership interest in the property.

2. ***Interest in the transaction.*** *A person has a direct or indirect interest in the transaction if, for example, the person or an affiliate of that person also serves as a loan officer of the creditor or otherwise arranges the credit transaction, or is the retail dealer of the manufactured home. A person also has a prohibited interest in the transaction if the person is compensated or otherwise receives financial or other benefits based on whether the transaction is consummated.*

3. ***Training in valuing manufactured homes.*** *Training in valuing manufactured homes includes, for example, successfully completing a course in valuing manufactured homes offered by a state or national appraiser association or receiving job training from an employer in the business of valuing manufactured homes.*

4. ***Manufactured home valuation - example.*** *A valuation in compliance with §1026.35(c)(2)(viii)(B)(3) would include, for example, an appraisal of the manufactured home in accordance with the appraisal requirements for a manufactured home classified as personal property under the Title I Manufactured Home Loan Insurance Program of the U.S. Department of Housing and Urban Development, pursuant to section 2(b)(10) of the National Housing Act, 12 U.S.C. 1703(b)(10).*

Appraisals - Appraisals Required - 12 CFR § 1026.35(c)(3)

Regulatory Discussion

This section states, in general, a creditor shall not extend a higher-priced mortgage loan without obtaining (prior to consummation) a written appraisal of the property to be mortgaged. Subject, of course, to the eight specific exemptions discussed previously under (c)(2)(i) through (viii).

In addition, the appraisal must be performed by a certified or licensed appraiser (defined in (c)(1)(i)) who conducts a physical visit of the interior of the collateral property.

Note the safe harbor protections.

Regulatory Text

(c) Appraisals.

(3) **Appraisals required**

(i) **In general.** Except as provided in paragraph (c)(2) of this section, a creditor shall not extend a higher-priced mortgage loan to a consumer without obtaining, prior to consummation, a written appraisal of the property to be mortgaged. The appraisal must be performed by a certified or licensed appraiser who conducts a physical visit of the interior of the property that will secure the transaction.

(ii) **Safe harbor.** A creditor obtains a written appraisal that meets the requirements for an appraisal required under paragraph (c)(3)(i) of this section if the creditor:

(A) 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, as amended (12 U.S.C. 3331 *et seq.*), and any implementing regulations in effect at the time the appraiser signs the appraiser's certification;

(B) 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;

(C) Confirms that the elements set forth in appendix N to this part are addressed in the written appraisal; and

(D) Has no actual knowledge contrary to the facts or certifications contained in the written appraisal.

Regulatory Commentary

35(c)(3) Appraisals Required

35(c)(3)(i) In General

*1. **Written appraisal - electronic transmission.** To satisfy the requirement that the appraisal be "written," a creditor may obtain the appraisal in paper form or via electronic transmission.*

35(c)(3)(ii) Safe Harbor.

*1. **Safe harbor.** A creditor that satisfies the safe harbor conditions in §1026.35(c)(3)(ii)(A) through (D) complies with the appraisal requirements of §1026.35(c)(3)(i). A creditor that does not satisfy the safe harbor conditions in §1026.35(c)(3)(ii)(A) through (D) does not necessarily violate the appraisal requirements of §1026.35(c)(3)(i).*

*2. **Appraiser's certification.** For purposes of §1026.35(c)(3)(ii), the appraiser's certification refers to the certification specified in item 9 of appendix N. See also comment 35(c)(1)(i)-2.*

Paragraph 35(c)(3)(ii)(C)

*1. **Confirming elements in the appraisal.** To confirm that the elements in appendix N to this part are included in the written appraisal, a creditor need not look beyond the face of the written appraisal and the appraiser's certification.*

Appraisals - Additional Appraisal for Certain HPMLs - 12 CFR § 1026.35(c)(4)

Regulatory Discussion

In the event either of the two circumstances described under (c)(4)(i)(A) or (B) occurs, two written appraisals are required. Items (c)(4)(ii) through (v) include additional requirements relative to the two appraisal requirement.

Item (c)(4)(vi) discusses a *potential exemption* if the creditor can can *demonstrate by exercising reasonable diligence* that the requirement to obtain two appraisals does not apply

Item (c)(4)(vii)(A) through (H) provides *eight actual exemptions* from the two appraisal requirement.

The commentary provides additional important information on every item, (i) through (vii).

Regulatory Text

(c) Appraisals.

(4) **Additional appraisal for certain higher-priced mortgage loans**

(i) **In general.** Except as provided in paragraphs (c)(2) and (c)(4)(vii) of this section, a creditor shall not extend a higher-priced mortgage loan to a consumer to finance the acquisition of the consumer's principal dwelling without obtaining, prior to consummation, two written appraisals, if:

(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 percent; 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 percent.

(ii) **Different certified or licensed appraisers.** The two appraisals required under paragraph (c)(4)(i) of this section may not be performed by the same certified or licensed appraiser.

(iii) **Relationship to general appraisal requirements.** If two appraisals must be obtained under paragraph (c)(4)(i) of this section, each appraisal shall meet the requirements of paragraph (c)(3)(i) of this section.

(iv) **Required analysis in the additional appraisal.** One of the two required appraisals 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, as specified in the consumer's agreement to acquire the property from 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.

(v) **No charge for the additional appraisal.** If the creditor must obtain two appraisals under paragraph (c)(4)(i) of this section, the creditor may charge the consumer for only one of the appraisals.

(vi) **Creditor's determination of prior sale date and price**

(A) **Reasonable diligence.** A creditor must obtain two written appraisals under paragraph (c)(4)(i) of this section unless the creditor can demonstrate by exercising reasonable diligence that the requirement to obtain two appraisals does not apply. A creditor acts with reasonable diligence if the creditor bases its determination on information contained in written source documents, such as the documents listed in Appendix O to this part.

(B) **Inability to determine prior sale date or price - modified requirements for additional appraisal.** If, after exercising reasonable diligence, a creditor cannot determine whether the conditions in paragraphs (c)(4)(i)(A) and (c)(4)(i)(B) are present and therefore must obtain two written appraisals in accordance with paragraphs (c)(4)(i) through (v) of this section, one of the two appraisals shall include an analysis of the factors in paragraph (c)(4)(iv) of this section only to the extent that the information necessary for the appraiser to perform the analysis can be determined.

(vii) **Exemptions from the additional appraisal requirement.** The additional appraisal required under paragraph (c)(4)(i) of this section shall not apply to extensions of credit that finance a consumer's acquisition of property:

(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, as defined in 50 U.S.C. App. 511(1), 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, if and for as long as the Federal financial institutions regulatory agencies, as defined in 12 U.S.C. 3350(6), waive the requirements in title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (12 U.S.C. 3331 *et seq*.), and any implementing regulations in that area; or

(H) Located in a rural county, as defined in 12 CFR 1026.35(b)(2)(iv)(A).

Regulatory Commentary

35(c)(4) Additional Appraisal for Certain Higher-Priced Mortgage Loans

1. ***Acquisition.*** *For purposes of §1026.35(c)(4), the terms "acquisition" and "acquire" refer to the acquisition of legal title to the property pursuant to applicable State law, including by purchase.*

35(c)(4)(i) In General

1. ***Appraisal from a previous transaction.*** *An appraisal that was previously obtained in connection with the seller's acquisition or the financing of the seller's acquisition of the property does not satisfy the requirements to obtain two written appraisals under §1026.35(c)(4)(i).*
2. ***90-day, 180-day calculation.*** *The time periods described in §1026.35(c)(4)(i)(A) and (B) are calculated by counting the day after the date on which the seller acquired the property, up to and including the date of the consumer's agreement to acquire the property that secures the transaction. For example, assume that the creditor determines that date of the consumer's acquisition agreement is October 15, 2012, and that the seller acquired the property on April 17, 2012. The first day to be counted in the 180-day calculation would be April 18, 2012, and the last day would be October 15, 2012. In this case, the number of days from April 17 would be 181, so an additional appraisal is not required.*
3. ***Date seller acquired the property.*** *For purposes of §1026.35(c)(4)(i)(A) and (B), the date on which the seller acquired the property is the date on which the seller became the legal owner of the property pursuant to applicable State law.*
4. ***Date of the consumer's agreement to acquire the property.*** *For the date of the consumer's agreement to acquire the property under §1026.35(c)(4)(i)(A) and (B), the creditor should use the date on which the consumer and the seller signed the agreement provided to the creditor by the consumer. The date on which the consumer and the seller signed the agreement might not be the date on which the consumer became contractually obligated under State law to acquire the property. For purposes of §1026.35(c)(4)(i)(A) and (B), a creditor is not obligated to determine whether and to what extent the agreement is legally binding on both parties. If the dates on which the consumer and the seller signed the agreement differ, the creditor should use the later of the two dates.*
5. ***Price at which the seller acquired the property.*** *The price at which the seller acquired the property refers to the amount paid by the seller to acquire the property. The price at which the seller acquired the property does not include the cost of financing the property.*
6. ***Price the consumer is obligated to pay to acquire the property.*** *The price the consumer is obligated to pay to acquire the property is the price indicated on the consumer's agreement with*

the seller to acquire the property. The price the consumer is obligated to pay to acquire the property from the seller does not include the cost of financing the property. For purposes of §1026.35(c)(4)(i)(A) and (B), a creditor is not obligated to determine whether and to what extent the agreement is legally binding on both parties. See also comment 35(c)(4)(i)-4.

35(c)(4)(ii) Different Certified or Licensed Appraisers

1. ***Independent appraisers.*** *The requirements that a creditor obtain two separate appraisals under §1026.35(c)(4)(i), and that each appraisal be conducted by a different licensed or certified appraiser under §1026.35(c)(4)(ii), indicate that the two appraisals must be conducted independently of each other. If the two certified or licensed appraisers are affiliated, such as by being employed by the same appraisal firm, then whether they have conducted the appraisal independently of each other must be determined based on the facts and circumstances of the particular case known to the creditor.*

35(c)(4)(iii) Relationship to General Appraisal Requirements

1. ***Safe harbor.*** *When a creditor is required to obtain an additional appraisal under §1026(c)(4)(i), the creditor must comply with the requirements of both §1026.35(c)(3)(i) and §1026.35(c)(4)(ii) through (v) for that appraisal. The creditor complies with the requirements of §1026.35(c)(3)(i) for the additional appraisal if the creditor meets the safe harbor conditions in §1026.35(c)(3)(ii) for that appraisal.*

35(c)(4)(iv) Required Analysis in the Additional Appraisal

1. ***Determining acquisition dates and prices used in the analysis of the additional appraisal.*** *For guidance on identifying the date on which the seller acquired the property, see comment 35(c)(4)(i)-3. For guidance on identifying the date of the consumer's agreement to acquire the property, see comment 35(c)(4)(i)-4. For guidance on identifying the price at which the seller acquired the property, see comment 35(c)(4)(i)-5. For guidance on identifying the price the consumer is obligated to pay to acquire the property, see comment 35(c)(4)(i)-6.*

35(c)(4)(v) No Charge for Additional Appraisal

1. ***Fees and mark-ups.*** *The creditor is prohibited from charging the consumer for the performance of one of the two appraisals required under §1026.35(c)(4)(i), including by imposing a fee specifically for that appraisal or by marking up the interest rate or any other fees payable by the consumer in connection with the higher-priced mortgage loan.*

35(c)(4)(vi) Creditor's Determination of Prior Sale Date and Price

35(c)(4)(vi)(A) In General

1. ***Estimated sales price.*** *If a written source document describes the seller's acquisition price in a manner that indicates that the price described is an estimated or assumed amount and not the actual price, the creditor should look at an alternative document to satisfy the reasonable diligence standard in determining the price at which the seller acquired the property.*

2. ***Reasonable diligence - oral statements insufficient.*** *Reliance on oral statements of interested parties, such as the consumer, seller, or mortgage broker, does not constitute reasonable diligence under §1026.35(c)(4)(vi)(A).*

3. ***Lack of information and conflicting information - two appraisals required.*** *If a creditor is unable to demonstrate that the requirement to obtain two appraisals under §1026.35(c)(4)(i) does not apply, the creditor must obtain two written appraisals before extending a higher-priced mortgage loan subject to the requirements of §1026.35(c). See also comment 35(c)(4)(vi)(B)-1. For example:*

   i. Assume a creditor orders and reviews the results of a title search, which shows that a prior sale occurred between 91 and 180 days ago, but not the price paid in that sale. Thus, based on the title search, the creditor would not be able to determine whether the price the consumer is obligated to pay under the consumer's acquisition agreement is more than 20 percent higher than the seller's acquisition price, pursuant to §1026.35(c)(4)(i)(B). Before extending a higher-priced mortgage loan subject to the appraisal requirements of §1026.35(c), the creditor must either: (1) Perform additional diligence to ascertain the seller's acquisition price and, based on this information, determine whether two written appraisals are required; or (2) obtain two written appraisals in compliance with §1026.35(c)(4). See also comment 35(c)(4)(vi)(B)-1.

   ii. Assume a creditor reviews the results of a title search indicating that the last recorded purchase was more than 180 days before the consumer's agreement to acquire the property. Assume also that the creditor subsequently receives a written appraisal indicating that the seller acquired the property between 91 and 180 days before the consumer's agreement to acquire the property. In this case, unless one of these sources is clearly wrong on its face, the creditor would not be able to determine whether the seller acquired the property within 180 days of the date of the consumer's agreement to acquire the property from the seller, pursuant to §1026.35(c)(4)(i)(B). Before extending a higher-priced mortgage loan subject to the appraisal requirements of §1026.35(c), the creditor must either: perform additional diligence to ascertain the seller's acquisition date and, based on this information, determine whether two written appraisals are required; or obtain two written appraisals in compliance with §1026.35(c)(4). See also comment 35(c)(4)(vi)(B)-1.

35(c)(4)(vi)(B) Inability To Determine Prior Sales Date or Price - Modified Requirements for Additional Appraisal

1. ***Required analysis.*** *In general, the additional appraisal required under §1026.35(c)(4)(i) should include an analysis of the factors listed in §1026.35(c)(4)(iv)(A) through (C). However, if, following reasonable diligence, a creditor cannot determine whether the conditions in §1026.35(c)(4)(i)(A) or (B) are present due to a lack of information or conflicting information, the required additional appraisal must include the analyses required under §1026.35(c)(4)(iv)(A) through (C) only to the extent that the information necessary to perform the analyses is known. For example, assume that a creditor is able, following reasonable diligence, to determine that the date on which the seller acquired the property occurred between 91 and 180 days prior to the date of the consumer's agreement to acquire the property. However, the creditor is unable, following reasonable diligence, to determine the price at which the seller acquired the property. In this case, the creditor is required to obtain an additional written appraisal that includes an analysis under §1026.35(c)(4)(iv)(B) and (c)(4)(iv)(C) of the changes in market conditions and 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. However, the creditor is not required to obtain an additional written appraisal that includes analysis under §1026.35(c)(4)(iv)(A) of 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.

35(c)(4)(vii) Exemptions From the Additional Appraisal Requirement

Paragraph 35(c)(4)(vii)(C)

*1. **Non-profit entity.** For purposes of §1026.35(c)(4)(vii)(C), a "non-profit entity" is a person with a tax exemption ruling or determination letter from the Internal Revenue Service under section 501(c)(3) of the Internal Revenue Code of 1986 (26 U.S.C. 501(c)(3)).*

Paragraph 35(c)(4)(vii)(H)

*1. **Bureau table of rural counties.** The Bureau publishes on its Web site a table of rural counties under §1026.35(c)(4)(vii)(H) for each calendar year by the end of that calendar year. See comment 35(b)(2)(iv)-1. A property securing an HPML subject to §1026.35(c) is in a rural county under §1026.35(c)(4)(vii)(H) if the county in which the property is located is on the table of rural counties most recently published by the Bureau. For example, for a transaction occurring in 2015, assume that the Bureau most recently published a table of rural counties at the end of 2014. The property securing the transaction would be located in a rural county for purposes of §1026.35(c)(4)(vii)(H) if the county is on the table of rural counties published by the Bureau at the end of 2014.*

Appraisals - Required Disclosure - 12 CFR § 1026.35(c)(5)

Regulatory Discussion

In general (except as provided in (c)(2), above), a specific disclosure must be provided, in writing, to a consumer who applies for a higher-priced mortgage loan.

In general, the disclosure must be delivered or placed in the mail no later than the third business day after the creditor receives the consumer's application (or is thereafter determined to be) for a higher-priced mortgage loan.

NOTE: compliance with the disclosure requirements in Regulation B will also satisfy the requirements of this section.

Regulatory Text

(c) Appraisals.

(5) **Required disclosure**

(i) **In general.** Except as provided in paragraph (c)(2) of this section, a creditor shall disclose the following statement, in writing, to a consumer who applies for a higher-priced mortgage loan: "We may order an appraisal to determine the property's value and charge you for this appraisal. We will give you a copy of any appraisal, even if your loan does not close. You can pay for an additional appraisal for your own use at your own cost." Compliance with the disclosure requirement in Regulation B, 12 CFR 1002.14(a)(2), satisfies the requirements of this paragraph.

(ii) **Timing of disclosure.** The disclosure required by paragraph (c)(5)(i) of this section shall be delivered or placed in the mail no later than the third business day after the creditor receives the consumer's application for a higher-priced mortgage loan subject to paragraph (c) of this section. In the case of a loan that is not a higher-priced mortgage loan subject to paragraph (c) of this section at the time of application, but becomes a higher-priced mortgage loan subject to paragraph (c) of this section after application, the disclosure shall be delivered or placed in the mail not later than the third business day after the creditor determines that the loan is a higher-priced mortgage loan subject to paragraph (c) of this section.

Regulatory Commentary

35(c)(5) Required Disclosure

35(c)(5)(i) In General

1. ***Multiple applicants.*** *When two or more consumers apply for a loan subject to this section, the creditor is required to give the disclosure to only one of the consumers.*

2. ***Appraisal independence requirements not affected.*** *Nothing in the text of the consumer notice required by §1026.35(c)(5)(i) should be construed to affect, modify, limit, or supersede the operation of any legal, regulatory, or other requirements or standards relating to independence in the conduct of appraisers or restrictions on the use of borrower-ordered appraisals by creditors.*

Appraisals – Copy of Appraisals - 12 CFR § 1026.35(c)(6)

Regulatory Discussion

This section requires the creditor to provide (at no cost) the consumer a copy (in electronic form subject to E-Sign Act) of any written appraisal associated with a higher-priced mortgage loan. The appraisal(s) must be provided no later than three business days prior to consummation; or in the event the loan is not consummated, no later than 30 days after it is know the loan will not be consummated.

Regulatory Text

(c) Appraisals.

(6) **Copy of appraisals**

(i) **In general.** Except as provided in paragraph (c)(2) of this section, a creditor shall provide to the consumer a copy of any written appraisal performed in connection with a higher-priced mortgage loan pursuant to paragraphs (c)(3) and (c)(4) of this section.

(ii) ***Timing.*** A creditor shall provide to the consumer a copy of each written appraisal pursuant to paragraph (c)(6)(i) of this section:

(A) No later than three business days prior to consummation of the loan; or

(B) In the case of a loan that is not consummated, no later than 30 days after the creditor determines that the loan will not be consummated.

(iii) **Form of copy.** Any copy of a written appraisal required by paragraph (c)(6)(i) of this section may be provided to the applicant in electronic form, subject to compliance with the consumer consent and other applicable provisions of the Electronic Signatures in Global and National Commerce Act (E-Sign Act) (15 U.S.C. 7001 *et seq.*).

(iv) **No charge for copy of appraisal.** A creditor shall not charge the consumer for a copy of a written appraisal required to be provided to the consumer pursuant to paragraph (c)(6)(i) of this section.

Regulatory Commentary

35(c)(6) Copy of Appraisals

35(c)(6)(i) In General

1. ***Multiple applicants.*** *When two or more consumers apply for a loan subject to this section, the creditor is required to give the copy of each required appraisal to only one of the consumers.*

35(c)(6)(ii) Timing

1. ***"Provide."*** *For purposes of the requirement to provide a copy of the appraisal within a specified time under §1026.35(c)(6)(ii), "provide" means "deliver." Delivery occurs three business days after mailing or delivering the copies to the last-known address of the applicant, or when evidence indicates actual receipt by the applicant (which, in the case of electronic receipt, must be based upon consent that complies with the E-Sign Act), whichever is earlier.*

2. ***No waiver.*** *Regulation B, 12 CFR 1002.14(a)(1), allowing the consumer to waive the requirement that the appraisal copy be provided three business days before consummation, does not apply to higher-priced mortgage loans subject to §1026.35(c). A consumer of a higher-priced mortgage loan subject to §1026.35(c) may not waive the timing requirement to receive a copy of the appraisal under §1026.35(c)(6)(i).*

35(c)(6)(iv) No Charge for Copy Of Appraisal

1. ***Fees and mark-ups.*** *The creditor is prohibited from charging the consumer for any copy of an appraisal required to be provided under §1026.35(c)(6)(i), 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.*

Appraisals - Relation to Other Rules - 12 CFR § 1026.35(c)(7)

Regulatory Discussion

This section simply states the appraisal rules are consistent among the various supervisory agencies.

Regulatory Text

(c) Appraisals.

(7) **Relation to other rules**. The rules in this paragraph (c) were adopted jointly by the Federal Reserve Board (Board), the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Federal Housing Finance Agency, and the Bureau. These rules are substantively identical to the Board's and the OCC's higher-priced mortgage loan appraisal rules published separately in 12 CFR 226.43 (for the Board) and in 12 CFR part 34, subpart G and 12 CFR part 164, subpart B (for the OCC).

Regulatory Commentary

None.

Section 4: Evasion; Open End Credit
12 C.F.R. § 1026.35(d)

Evasion; Open End Credit - 12 CFR § 1026.35(d)

Regulatory Discussion

This section simply states a creditor shall not structure a home-secured loan as an open-end plan to evade the higher-priced mortgage transaction requirements of this section.

Regulatory Text

(d) **Evasion; open-end credit.** In connection with credit secured by a consumer's principal dwelling that does not meet the definition of open-end credit in §1026.2(a)(20), a creditor shall not structure a home-secured loan as an open-end plan to evade the requirements of this section.

Regulatory Commentary

None.

Prohibited Acts or Practices and Certain Requirements for Credit Secured by a Dwelling

Section 1: Definitions
12 C.F.R. § 1026.36(a)

Loan Originator - 12 CFR § 1026.36(a)(1)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) **Loan originator.**

(i) For purposes of this section, the term "loan originator" means a person who, in expectation of direct or indirect compensation or other monetary gain or for direct or indirect compensation or other monetary gain, performs any of the following activities: takes an application, offers, arranges, assists a consumer in obtaining or applying to obtain, negotiates, or otherwise obtains or makes an extension of consumer credit for another person; or through advertising or other means of communication represents to the public that such person can or will perform any of these activities. The term "loan originator" includes an employee, agent, or contractor of the creditor or loan originator organization if the employee, agent, or contractor meets this definition. The term "loan originator" includes a creditor that engages in loan origination activities if the creditor does not finance the transaction at consummation out of the creditor's own resources, including by drawing on a *bona fide* warehouse line of credit or out of deposits held by the creditor. All creditors that engage in any of the foregoing loan origination activities are loan originators for purposes of paragraphs (f) and (g) of this section. The term does not include:

(A) A person who does not take a consumer credit application or offer or negotiate credit terms available from a creditor, but who performs purely administrative or clerical tasks on behalf of a person who does engage in such activities.

(B) An employee of a manufactured home retailer who does not take a consumer credit application, offer or negotiate credit terms available from a creditor, or advise a consumer on credit terms (including rates, fees, and other costs) available from a creditor.

(C) A person that performs only real estate brokerage activities and is licensed or registered in accordance with applicable State law, unless such person is compensated by a creditor or loan originator or by any agent of such creditor or loan originator for a particular consumer credit transaction subject to this section.

(D) A seller financer that meets the criteria in paragraph (a)(4) or (a)(5) of this section, as applicable.

(E) A servicer or servicer's employees, agents, and contractors who offer or negotiate terms for purposes of renegotiating, modifying, replacing, or subordinating principal of existing mortgages where consumers are behind in their payments, in default, or have a reasonable likelihood of defaulting or falling behind. This exception does not apply, however, to a servicer or servicer's employees, agents, and contractors who offer or negotiate a transaction that constitutes a refinancing under §1026.20(a) or obligates a different consumer on the existing debt.

(ii) An **"individual loan originator"** is a natural person who meets the definition of "loan originator" in paragraph (a)(1)(i) of this section.

(iii) A **"loan originator organization"** is any loan originator, as defined in paragraph (a)(1)(i) of this section, that is not an individual loan originator.

Regulatory Commentary

*1. **Meaning of loan originator.***

*i. **General.***

A. Section 1026.36(a) defines the set of activities or services any one of which, if done for or in the expectation of compensation or gain, makes the person doing such activities or performing such services a loan originator, unless otherwise excluded. The scope of activities covered by the term loan originator includes:

1. Referring a consumer to any person who participates in the origination process as a loan originator. Referring is an activity included under each of the activities of offering, arranging, or assisting a consumer in obtaining or applying to obtain an extension of credit. Referring includes any oral or written action directed to a consumer that can affirmatively influence the consumer to select a particular loan originator or creditor to obtain an extension of credit when the consumer will pay for such credit. See comment 36(a)-4 with respect to certain activities that do not constitute referring.

2. Arranging a credit transaction, including initially contacting and orienting the consumer to a particular loan originator's or creditor's origination process or particular credit terms that are or may be available to that consumer selected based on the consumer's financial characteristics, assisting the consumer to apply for credit, taking an application, offering particular credit terms to the consumer selected based on the consumer's financial characteristics, negotiating credit terms, or otherwise obtaining or making an extension of credit.

3. Assisting a consumer in obtaining or applying for consumer credit by advising on particular credit terms that are or may be available to that consumer based on the consumer's financial characteristics, filling out an application form, preparing application packages (such as a credit application or pre-approval application or supporting documentation), or collecting application and supporting information on behalf of the consumer to submit to a loan originator or creditor. A person who, acting on behalf of a loan originator or creditor, collects information or verifies information provided by the consumer, such as by asking the consumer for documentation to support the information the consumer provided or for the consumer's authorization to obtain supporting documents from third parties, is not *collecting information on behalf of the consumer. See also comment **36**(a)-4.i through .iv with respect to application-related administrative and clerical tasks and comment **36**(a)-1.v with respect to third-party advisors.*

4. Presenting particular credit terms for the consumer's consideration that are selected based on the consumer's financial characteristics, or communicating with a consumer for the purpose of reaching a mutual understanding about prospective credit terms.

5. Advertising or communicating to the public that one can or will perform any loan origination services. Advertising the services of a third party that engages or intends to engage in loan origination activities does not make the advertiser a loan originator.

B. The term "loan originator" includes employees, agents, and contractors of a creditor as well as employees, agents, and contractors of a mortgage broker that satisfy this definition.

*C. The term "loan originator" includes any creditor that satisfies the definition of loan originator but makes use of "table funding" by a third party. See comment **36**(a)-1.ii discussing table funding. Solely for purposes of §**1026.36**(f) and (g) concerning loan originator qualifications, the term loan originator includes any creditor that satisfies the definition of loan originator, even if the creditor does not make use of table funding. Such a person is a creditor, not a loan originator, for general purposes of this part, including the provisions of §**1026.36** other than §**1026.36**(f) and (g).*

*D. A "loan originator organization" is a loan originator other than a natural person. The term includes any legal person or organization such as a sole proprietorship, trust, partnership, limited liability partnership, limited partnership, limited liability company, corporation, bank, thrift, finance company, or credit union. An "individual loan originator" is limited to a natural person. (Under §**1026.2**(a)(22), the term "person" means a natural person or an organization.)*

E. The term "loan originator" does not include consumers who obtain extensions of consumer credit on their own behalf.

*ii. **Table funding.** Table funding occurs when the creditor does not provide the funds for the transaction at consummation out of the creditor's own resources, including, for example, by drawing on a bona fide warehouse line of credit or out of deposits held by the creditor. Accordingly, a table-funded transaction is consummated with the debt obligation initially payable by its terms to one person, but another person provides the funds for the transaction at consummation and receives an immediate assignment of the note, loan contract, or other evidence of the debt obligation. Although §**1026.2**(a)(17)(i)(B) provides that a person to whom a debt obligation is initially payable on its face generally is a creditor, §**1026.36**(a)(1) provides that, solely for the purposes of §**1026.36**, such a person is also considered a loan originator. For example, if a person closes a transaction in its own name but does not fund the transaction from its own resources and assigns the transaction after consummation to the person providing the funds, it is considered a creditor for purposes of Regulation Z and also a loan originator for purposes of §**1026.36**. However, if a person closes in its own name and finances a consumer credit transaction from the person's own resources, including* *drawing on a bona fide warehouse line of credit or out of deposits held by the person, and does not assign the loan at closing, the person is a creditor not making use of table funding but is included in the definition of loan originator for the purposes of §1026.36(f) and (g) concerning loan originator qualifications.*

*iii. **Servicing.** A loan servicer or a loan servicer's employees, agents, or contractors that otherwise meet the definition of "loan originator" are excluded from the definition when modifying or offering to modify an existing loan on behalf of the current owner or holder of the loan (including an assignee or the servicer, if applicable). Other than §1026.36(c), §1026.36 applies to extensions of consumer credit. Thus, other than §1026.36(c), §1026.36 does not apply if a person renegotiates, modifies, replaces, or subordinates an existing obligation or its terms, unless the transaction constitutes a refinancing under §1026.20(a) or obligates a different consumer on the existing debt.*

*iv. **Real estate brokerage.** The definition of "loan originator" does not include a person that performs only real estate brokerage activities (e.g., does not perform mortgage broker or consumer credit referral activities or extend consumer credit) if the person is licensed or registered under applicable State law governing real estate brokerage, unless such person is paid by a loan originator or a creditor for a particular consumer credit transaction subject to §1026.36. Such a person is not paid by a loan originator or a creditor if the person is paid by a loan originator or creditor on behalf of a buyer or seller solely for performing real estate brokerage activities. Such a person is not paid for a particular consumer credit transaction subject to §1026.36 if the person is paid compensation by a loan originator or creditor, or affiliate of the loan originator or creditor, solely for performing real estate brokerage activities in connection with a property owned by that loan originator or creditor.*

*v. **Third-party advisors.** [Omitted.]*

*2. **Meaning of mortgage broker.** For purposes of §1026.36, with respect to a particular transaction, the term "mortgage broker" refers to a loan originator who is not an employee of the creditor. Accordingly, the term "mortgage broker" includes companies that engage in the activities described in §1026.36(a) and also includes employees of such companies that engage in these activities. Section 1026.36(d) prohibits certain payments to a loan originator. These prohibitions apply to payments made to all loan originators, including payments made to mortgage brokers, and payments made by a company acting as a mortgage broker to its employees who are loan originators.*

*3. **Meaning of creditor**. For purposes of §1026.36(d) and (e), a creditor means a creditor that is not deemed to be a loan originator on the transaction under this section. Thus, a person that closes a loan in its own name (but another person provides the funds for the transaction at consummation and receives an immediate assignment of the note, loan contract, or other evidence of the debt obligation) is deemed a loan originator, not a creditor, for purposes of §1026.36. However, that person is still a creditor for all other purposes of Regulation Z.*

*4. **Managers, administrative and clerical staff.** For purposes of §1026.36, managers, administrative and clerical staff, and similar individuals who are employed by (or contractor or agent of) a creditor or loan originator organization and take an application, offer, arrange, assist a consumer in obtaining or applying to obtain, negotiate, or otherwise obtain or make a particular extension of credit for another person are loan originators. The following examples describe activities that, in the absence of any other activities, do not render a manager, administrative or clerical staff member, or similar employee a loan originator:*

i. Application-related administrative and clerical tasks. The definition of loan originator does not include a loan originator's or creditor's employee who provides a credit application form from the entity for which the person works to the consumer for the consumer to complete or, without assisting the consumer in completing the credit application, processing or analyzing the information, or discussing particular credit terms that are or may be available from a creditor or loan originator to that consumer selected based on the consumer's financial characteristics, delivers the credit application from a consumer to a loan originator or creditor. A person does not assist the consumer in completing the application if the person explains to the consumer filling out the application the contents of the application or where particular consumer information is to be provided, or generally describes the credit application process to a consumer without discussing particular credit terms that are or may be available from a creditor or loan originator to that consumer selected based on the consumer's financial characteristics.

ii. Responding to consumer inquiries and providing general information. The definition of loan originator does not include persons who:

A. Provide general explanations, information, or descriptions in response to consumer queries, such as explaining credit terminology or lending policies or who confirm written offer terms already transmitted to the consumer;

B. As employees of a creditor or loan originator, provide loan originator or creditor contact information of the loan originator or creditor entity for which he or she works, or of a person who works for that the same entity to a consumer, provided that the person does not discuss particular credit terms that are or may be available from a creditor or loan originator to that consumer selected based on the consumer's financial characteristics and does not direct the consumer, based on his or her assessment of the consumer's financial characteristics, to a particular loan originator or particular creditor seeking to originate credit transactions to consumers with those financial characteristics;

C. Describe other product-related services (for example, persons who describe optional monthly payment methods via telephone or via automatic account withdrawals, the availability and features of online account access, the availability of 24-hour customer support, or free mobile applications to access account information); or

D. Explain or describe the steps that a consumer would need to take to obtain an offer of credit, including providing general guidance on qualifications or criteria that would need to be met that is not specific to that consumer's circumstances.

*iii. **Loan processing.** The definition of loan originator does not include persons who, acting on behalf of a loan originator or a creditor:*

A. Compile and assemble credit application packages and supporting documentation;

B. Verify information provided by the consumer in a credit application such as by asking the consumer for supporting documentation or the consumer's authorization for the person to obtain supporting documentation from other persons;

C. Coordinate consummation of the credit transaction or other aspects of the credit transaction process, including by communicating with a consumer about process deadlines and documents needed at consummation, provided that any communication that includes a discussion about credit terms available from a creditor to that consumer *selected based on the consumer's financial characteristics only confirms credit terms already agreed to by the consumer;*

D. Provide a consumer with information unrelated to credit terms, such as the best days of the month for scheduling consummation; or

E. Communicate on behalf of a loan originator that a written credit offer has been sent to a consumer without providing any details of that offer.

iv. ***Underwriting, credit approval, and credit pricing.*** *The definition of loan originator does not include persons who:*

A. Receive and evaluate a consumer's information to make underwriting decisions on whether a consumer qualifies for an extension of credit and communicate decisions to a loan originator or creditor, provided that only a loan originator communicates such underwriting decisions to the consumer;

B. Approve particular credit terms or set particular credit terms available from a creditor to that consumer selected based on the consumer's financial characteristics in offer or counter-offer situations, provided that only a loan originator communicates to or with the consumer regarding these credit terms, an offer, or provides or engages in negotiation, a counter-offer, or approval conditions; or

C. Establish credit pricing that the creditor offers generally to the public, via advertisements or other marketing or via other persons that are loan originators.

v. ***Producing managers.*** *Managers that work for creditors or loan originator organizations sometimes engage themselves in loan origination activities, as set forth in the definition of loan originator in §1026.36(a)(1)(i) (such managers are sometimes referred to as "producing managers"). The definition of loan originator includes persons, including managers, who are employed by a creditor or loan originator organization and take an application, offer, arrange, assist a consumer with obtaining or applying to obtain, negotiate, or otherwise obtain or make a particular extension of credit for another person, even if such persons are also employed by the creditor or loan originator organization to perform duties that are not loan origination activities. Thus, such producing managers are loan originators.*

5. ***Compensation.***

i. ***General.*** *For purposes of §1026.36, compensation is defined in §1026.36(a)(3) as salaries, commissions, and any financial or similar incentive. For example, the term "compensation" includes:*

A. An annual or other periodic bonus; or

B. Awards of merchandise, services, trips, or similar prizes.

ii. ***Name of fee.*** *Compensation includes amounts the loan originator retains and is not dependent on the label or name of any fee imposed in connection with the transaction. For example, if a loan originator imposes a "processing fee" in connection with the transaction and retains such fee, it is compensation for purposes of §1026.36, including §1026.36(d) and (e), whether the originator expends the time to process the consumer's application or uses the fee for other expenses, such as overhead.*

iii. ***Amounts for third-party charges.*** *Compensation does not include amounts the loan originator receives as payment for bona fide and reasonable charges, such as credit reports, where those amounts are passed on to a third party that is not the creditor, its affiliate, or the affiliate of the loan originator. See comment 36(a)-5.v.*

iv. Amounts for charges for services that are not loan origination activities.

1. A payment received by a loan originator organization for bona fide and reasonable charges for services it performs that are not loan origination activities;

2. A payment received by an affiliate of a loan originator organization for bona fide and reasonable charges for services it performs that are not loan origination activities; or

3. A payment received by a loan originator organization for bona fide and reasonable charges for services that are not loan origination activities where those amounts are not retained by the loan originator but are paid to the creditor, its affiliate, or the affiliate of the loan originator organization. See comment 36(a)-5.v.

B. Compensation includes any salaries, commissions, and any financial or similar incentive to an individual loan originator, regardless of whether it is labeled as payment for services that are not loan origination activities.

C. Loan origination activities for purposes of this comment means activities described in §1026.36(a)(1)(i) (e.g., taking an application, offering, arranging, negotiating, or otherwise obtaining an extension of consumer credit for another person) that would make a person performing those activities for compensation a loan originator as defined in §1026.36(a)(1)(i).

v. ***Amounts that exceed the actual charge for a service****. In some cases, amounts received by the loan originator organization for payment for third-party charges described in comment 36(a)-5.iii or payment for services to the creditor, its affiliates, or the affiliates of the loan originator organization described in comment 36(a)-5.iv.A.3 may exceed the actual charge because, for example, the loan originator organization cannot determine with accuracy what the actual charge will be when it is imposed and instead uses average charge pricing (in accordance with the Real Estate Settlement Procedures Act). In such a case, the difference retained by the loan originator organization is not compensation if the charge imposed on the consumer or collected from a person other than the consumer was bona fide and reasonable and also complies with State and other applicable law. On the other hand, if the loan originator organization marks up the charge (a practice known as "upcharging"), and the originator retains the difference between the actual charge and the marked-up charge, the amount retained is compensation for purposes of §1026.36, including §1026.36(d) and (e). For example:*

A. Assume a loan originator organization receives compensation directly from either a consumer or a creditor. Further assume the loan originator organization uses average charge pricing in accordance with the Real Estate Settlement Procedures Act and, based on its past average cost for credit reports, charges the consumer $25 for a credit report provided by a third party. Under the loan originator organization's agreement with the consumer reporting agency, the cost of the credit report is to be paid in a month-end bill and will vary between $15 and $35 depending on how many credit reports the originator obtains that month. Assume the $25 for the credit report is paid by the consumer or is *paid by the creditor with proceeds from a rebate. At the end of the month, the cost for the credit report is determined to be $15 for this consumer's transaction, based on the loan originator organization's credit report volume that month. In this case, the $10 difference between the $25 credit report fee imposed on the consumer and the actual $15 cost for the credit report is not compensation for purposes of §1026.36, even though the $10 is retained by the loan originator organization.*

B. Using the same example as in comment 36(a)-5.v.A, the $10 difference would be compensation for purposes of §1026.36 if the price for a credit report varies between $10 and $15.

*vi. **Returns on equity interests and dividends on equity holdings.** The term "compensation" for purposes of §1026.36(d) and (e) also includes, for example, awards of stock, stock options and equity interests. Thus, the awarding of stock, stock options, or equity interests to loan originators is subject to the restrictions in §1026.36(d) and (e). For example, a person may not award additional stock or a preferable type of equity interest to a loan originator based on the terms of a consumer credit transaction subject to §1026.36 originated by that loan originator. However, bona fide returns or dividends paid on stock or other equity holdings, including those paid to owners or shareholders of a loan originator organization who own such stock or equity interests, are not compensation for purposes of §1026.36(d) and (e). Bona fide returns or dividends are those returns and dividends that are paid pursuant to documented ownership or equity interests and that are not functionally equivalent to compensation. Ownership and equity interests must be bona fide. Bona fide ownership and equity interests are allocated according to a loan originator's respective capital contribution where the allocation is not a mere subterfuge for the payment of compensation based on terms of a transaction. Ownership and equity interests also are not bona fide if the formation or maintenance of the business from which returns or dividends are paid is a mere subterfuge for the payment of compensation based on the terms of a transaction. For example, assume that three individual loan originators form a loan originator organization that is a limited liability company (LLC). The three individual loan originators are members of the LLC, and the LLC agreement governing the loan originator organization's structure calls for regular distributions based on the members' respective equity interests. If the members' respective equity interests are allocated based on the members' terms of transactions, rather than according to their respective capital contributions, then distributions based on such equity interests are not bona fide and, thus, are compensation for purposes of §1026.36(d) and (e).*

36(a)(1)(i)(B) Employee of a retailer of manufactured homes.

[Omitted]

Mortgage Broker - 12 CFR § 1026.36(a)(2)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(2) **Mortgage broker.** For purposes of this section, a mortgage broker with respect to a particular transaction is any loan originator that is not an employee of the creditor.

Regulatory Commentary

None.

Compensation - 12 CFR § 1026.36(a)(3)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(3) **Compensation.** The term "compensation" includes salaries, commissions, and any financial or similar incentive.

Regulatory Commentary

None.

Seller Financers; Three Properties - 12 CFR § 1026.36(a)(4)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(4) **Seller financers; three properties.** A person (as defined in §1026.2(a)(22)) that meets all of the following criteria is not a loan originator under paragraph (a)(1) of this section:

(i) The person provides seller financing for the sale of three or fewer properties in any 12-month period to purchasers of such properties, each of which is owned by the person and serves as security for the financing.

(ii) The person has not constructed, or acted as a contractor for the construction of, a residence on the property in the ordinary course of business of the person.

(iii) The person provides seller financing that meets the following requirements:

(A) The financing is fully amortizing.

(B) The financing is one that the person determines in good faith the consumer has a reasonable ability to repay.

(C) The financing has a fixed rate or an adjustable rate that is adjustable after five or more years, subject to reasonable annual and lifetime limitations on interest rate increases. If the financing agreement has an adjustable rate, the rate is determined by the addition of a margin to an index rate and is subject to reasonable rate adjustment limitations. The index the adjustable rate is based on is a widely available index such as indices for U.S. Treasury securities or LIBOR.

Regulatory Commentary

[Omitted]

Seller Financers; One Property - 12 CFR § 1026.36(a)(5)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(5) ***Seller financers; one property.*** A natural person, estate, or trust that meets all of the following criteria is not a loan originator under paragraph (a)(1) of this section:

(i) The natural person, estate, or trust provides seller financing for the sale of only one property in any 12-month period to purchasers of such property, which is owned by the natural person, estate, or trust and serves as security for the financing.

(ii) The natural person, estate, or trust has not constructed, or acted as a contractor for the construction of, a residence on the property in the ordinary course of business of the person.

(iii) The natural person, estate, or trust provides seller financing that meets the following requirements:

(A) The financing has a repayment schedule that does not result in negative amortization.

(B) The financing has a fixed rate or an adjustable rate that is adjustable after five or more years, subject to reasonable annual and lifetime limitations on interest rate increases. If the financing agreement has an adjustable rate, the rate is determined by the addition of a margin to an index rate and is subject to reasonable rate adjustment limitations. The index the adjustable rate is based on is a widely available index such as indices for U.S. Treasury securities or LIBOR.

Regulatory Commentary

[Omitted.]

Credit Terms - 12 CFR § 1026.36(a)(6)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(6) **Credit terms.** For purposes of this section, the term “credit terms” includes rates, fees, and other costs. Credit terms are selected based on the consumer's financial characteristics when those terms are selected based on any factors that may influence a credit decision, such as debts, income, assets, or credit history.

Regulatory Commentary

None.

Scope - 12 CFR § 1026.36(b)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(b) **Scope.** Paragraphs (c)(1) and (2) of this section apply to closed-end consumer credit transactions secured by a consumer's principal dwelling. Paragraph (c)(3) of this section applies to a consumer credit transaction secured by a dwelling. Paragraphs (d) through (i) of this section apply to closed-end consumer credit transactions secured by a dwelling. This section does not apply to a home equity line of credit subject to §1026.40, except that paragraphs (h) and (i) of this section apply to such credit when secured by the consumer's principal dwelling and paragraph (c)(3) applies to such credit when secured by a dwelling. Paragraphs (d) through (i) of this section do not apply to a loan that is secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53D).

Regulatory Commentary

36(b) Scope.

*1. **Scope of coverage.** Section 1026.36(c)(1) and (c)(2) applies to closed-end consumer credit transactions secured by a consumer's principal dwelling. Section 1026.36(c)(3) applies to a consumer credit transaction, including home equity lines of credit under §1026.40, secured by a consumer's dwelling. Paragraphs (h) and (i) of §1026.36 apply to home equity lines of credit under §1026.40 secured by a consumer's principal dwelling. Paragraphs (d), (e), (f), (g), (h), and (i) of §1026.36 apply to closed-end consumer credit transactions secured by a dwelling. Closed-end consumer credit transactions include transactions secured by first or subordinate liens, and reverse mortgages that are not home equity lines of credit under §1026.40. See §1026.36(b) for additional restrictions on the scope of §1026.36, and §§1026.1(c) and 1026.3(a) and corresponding commentary for further Regulatory Discussion of extensions of credit subject to Regulation Z.*

Servicing Practices - 12 CFR § 1026.36(c)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(c) **Servicing practices.** For purposes of this paragraph (c), the terms “servicer” and “servicing” have the same meanings as provided in 12 CFR 1024.2(b).

(1) **Payment processing.** In connection with a consumer credit transaction secured by a consumer's principal dwelling:

(i) **Periodic payments**. No servicer shall fail to credit a periodic payment to the consumer's loan account as of the date of receipt, except when a delay in crediting does not result in any charge to the consumer or in the reporting of negative information to a consumer reporting agency, or except as provided in paragraph (c)(1)(iii) of this section. A periodic payment, as used in this paragraph (c), is an amount sufficient to cover principal, interest, and escrow (if applicable) for a given billing cycle. A payment qualifies as a periodic payment even if it does not include amounts required to cover late fees, other fees, or non-escrow payments a servicer has advanced on a consumer's behalf.

(ii) **Partial payments.** Any servicer that retains a partial payment, meaning any payment less than a periodic payment, in a suspense or unapplied funds account shall:

(A) Disclose to the consumer the total amount of funds held in such suspense or unapplied funds account on the periodic statement as required by §1026.41(d)(3), if a periodic statement is required; and

(B) On accumulation of sufficient funds to cover a periodic payment in any suspense or unapplied funds account, treat such funds as a periodic payment received in accordance with paragraph (c)(1)(i) of this section.

(iii) **Non-conforming payments.** If a servicer specifies in writing requirements for the consumer to follow in making payments, but accepts a payment that does not conform to the requirements, the servicer shall credit the payment as of five days after receipt.

(2) **No pyramiding of late fees.** In connection with a consumer credit transaction secured by a consumer's principal dwelling, a servicer shall not impose any late fee or delinquency charge for a payment if:

(i) Such a fee or charge is attributable solely to failure of the consumer to pay a late fee or delinquency charge on an earlier payment; and

(ii) The payment is otherwise a periodic payment received on the due date, or within any applicable courtesy period.

(3) **Payoff statements.** In connection with a consumer credit transaction secured by a consumer's dwelling, a creditor, assignee or servicer, as applicable, must provide an accurate statement of the total outstanding balance that would be required to pay the consumer's obligation in full as of a specified date. The statement shall be sent within a reasonable time, but in no case more than seven business days, after receiving a written request from the consumer or any person acting on behalf of the consumer. When a creditor, assignee, or servicer, as applicable, is not able to provide the statement within seven business days of such a request because a loan is in bankruptcy or foreclosure, because the loan is a reverse mortgage or shared appreciation mortgage, or because of natural disasters or other similar circumstances, the payoff statement must be provided within a reasonable time. A creditor or assignee that does not currently own the mortgage loan or the mortgage servicing rights is not subject to the requirement in this paragraph (c)(3) to provide a payoff statement.

Regulatory Commentary

[Omitted.]

Section 4: Prohibited Payments to Loan Originators 12 C.F.R. § 1026.36(d)

Prohibited Payments to Loan Originators - 12 C.F.R. § 1026.36(d)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) **Payments based on a term of a transaction.**

(i) Except as provided in paragraph (d)(1)(iii) or (iv) of this section, in connection with a consumer credit transaction secured by a dwelling, no loan originator shall receive and no person shall pay to a loan originator, directly or indirectly, compensation in an amount that is 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. 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. 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.

(ii) For purposes of this paragraph (d)(1) only, a "term of a transaction" is any right or obligation of the parties to a credit transaction. 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; however, such compensation may be subject to a minimum or maximum dollar amount.

(iii) An individual loan originator may receive, and a person may pay to an individual loan originator, compensation in the form of a contribution to a defined contribution plan that is a designated tax-advantaged plan or a benefit under a defined benefit plan that is a designated tax-advantaged plan. In the case of a contribution to a defined contribution plan, the contribution shall not be directly or indirectly based on the terms of that individual loan originator's transactions. As used in this paragraph (d)(1)(iii), "designated tax-advantaged plan" means any plan that meets the requirements of Internal Revenue Code section 401(a), 26 U.S.C. 401(a); employee annuity plan described in Internal Revenue Code section 403(a), 26 U.S.C. 403(a); simple retirement account, as defined in Internal Revenue Code section 408(p), 26 U.S.C. 408(p); simplified employee pension described in Internal Revenue Code section 408(k), 26 U.S.C. 408(k); annuity contract described in Internal Revenue Code section 403(b), 26 U.S.C. 403(b); or eligible deferred compensation plan, as defined in Internal Revenue Code section 457(b), 26 U.S.C. 457(b).

(iv) An individual loan originator may receive, and a person may pay to an individual loan originator, compensation under a non-deferred profits-based compensation plan (*i.e.,* any arrangement for the payment of non-deferred compensation that is determined with reference to the profits of the person from mortgage-related business), provided that:

(A) The compensation paid to an individual loan originator pursuant to this paragraph (d)(1)(iv) is not directly or indirectly based on the terms of that individual loan originator's transactions that are subject to this paragraph (d); and

(B) At least one of the following conditions is satisfied:

(1) The compensation paid to an individual loan originator pursuant to this paragraph (d)(1)(iv) does not, in the aggregate, exceed 10 percent of the individual loan originator's total compensation corresponding to the time period for which the compensation under the non-deferred profits-based compensation plan is paid; or

(2) The individual loan originator was a loan originator for ten or fewer transactions subject to this paragraph (d) consummated during the 12-month period preceding the date of the compensation determination.

(2) **Payments by persons other than consumer**

(i) **Dual compensation.**

(A) Except as provided in paragraph (d)(2)(i)(C) of this section, if any loan originator receives compensation directly from a consumer in a consumer credit transaction secured by a dwelling:

(1) No loan originator shall receive compensation, directly or indirectly, from any person other than the consumer in connection with the transaction; and

(2) 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.

(B) 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).

(C) If a loan originator organization receives compensation directly from a consumer in connection with a transaction, the loan originator organization may pay compensation to an individual loan originator, and the individual loan originator may receive compensation from the loan originator organization, subject to paragraph (d)(1) of this section.

(ii) **Exemption.** A payment to a loan originator that is otherwise prohibited by section 129B(c)(2)(A) of the Truth in Lending Act is nevertheless permitted pursuant to section 129B(c)(2)(B) of the Act, regardless of whether the consumer makes any upfront payment of discount points, origination points, or fees, as described in section 129B(c)(2)(B)(ii) of the Act, as long as the loan originator does not receive any compensation directly from the consumer as described in section 129B(c)(2)(B)(i) of the Act.

(3) **Affiliates.** For purposes of this paragraph (d), affiliates shall be treated as a single "person."

Regulatory Commentary

[Omitted.]

Section 5: Prohibition on Steering
12 C.F.R. § 1026.36(e)

Prohibition on Steering - 12 CFR § 1026.36(e)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) **General.** In connection with a consumer credit transaction secured by a dwelling, a loan originator shall not direct or "steer" a consumer to consummate a transaction based on the fact that the originator will receive greater compensation from the creditor in that transaction than in other transactions the originator offered or could have offered to the consumer, unless the consummated transaction is in the consumer's interest.

(2) **Permissible transactions.** A transaction does not violate paragraph (e)(1) of this section if the consumer is presented with loan options that meet the conditions in paragraph (e)(3) of this section for each type of transaction in which the consumer expressed an interest. For purposes of paragraph (e) of this section, the term "type of transaction" refers to whether:

(i) A loan has an annual percentage rate that cannot increase after consummation;

(ii) A loan has an annual percentage rate that may increase after consummation; or

(iii) A loan is a reverse mortgage.

(3) **Loan options presented.** A transaction satisfies paragraph (e)(2) of this section only if the loan originator presents the loan options required by that paragraph and all of the following conditions are met:

(i) The loan originator must obtain loan options from a significant number of the creditors with which the originator regularly does business and, for each type of transaction in which the consumer expressed an interest, must present the consumer with loan options that include:

(A) The loan with the lowest interest rate;

(B) The loan with the lowest interest rate without negative amortization, a prepayment penalty, interest-only payments, a balloon payment in the first 7 years of the life of the loan, a demand feature, shared equity, or shared appreciation; or, in the case of a reverse mortgage, a loan without a prepayment penalty, or shared equity or shared appreciation; and

(C) The loan with the lowest total dollar amount of discount points, origination points or origination fees (or, if two or more loans have the same total dollar amount of discount points, origination points or origination fees, the loan with the lowest interest rate that has the lowest total dollar amount of discount points, origination points or origination fees).

(ii) The loan originator must have a good faith belief that the options presented to the consumer pursuant to paragraph (e)(3)(i) of this section are loans for which the consumer likely qualifies.

(iii) For each type of transaction, if the originator presents to the consumer more than three loans, the originator must highlight the loans that satisfy the criteria specified in paragraph (e)(3)(i) of this section.

(4) **Number of loan options presented.** The loan originator can present fewer than three loans and satisfy paragraphs (e)(2) and (e)(3)(i) of this section if the loan(s) presented to the consumer satisfy the criteria of the options in paragraph (e)(3)(i) of this section and the provisions of paragraph (e)(3) of this section are otherwise met.

Regulatory Commentary

[Omitted.]

Section 6: Loan Originator Qualifications
12 C.F.R. § 1026.36(f)

Loan Originator Qualifications - 12 CFR § 1026.36(f)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(f) **Loan originator qualification requirements.** A loan originator for a consumer credit transaction secured by a dwelling must, when required by applicable State or Federal law, be registered and licensed in accordance with those laws, including the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act, 12 U.S.C. 5102 *et seq.*), its implementing regulations (12 CFR part 1007 or part 1008), and State SAFE Act implementing law. To comply with this paragraph (f), a loan originator organization that is not a government agency or State housing finance agency must:

(1) Comply with all applicable State law requirements for legal existence and foreign qualification;

(2) Ensure that each individual loan originator who works for the loan originator 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 implementing law before the individual acts as a loan originator in a consumer credit transaction secured by a dwelling; 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 pursuant to §1008.103 of this chapter or State SAFE Act implementing law:

(i) Obtain for any individual whom the loan originator organization hired on or after January 1, 2014 (or whom the loan originator organization hired before this date but for whom there were no applicable statutory or regulatory background standards in effect at the time of hire or before January 1, 2014, used to screen the individual) and for any individual regardless of when hired who, based on reliable information known to the loan originator organization, likely does not meet the standards under §1026.36(f)(3)(ii), before the individual acts as a loan originator in a consumer credit transaction secured by a dwelling:

(A) A criminal background check through the Nationwide Mortgage Licensing System and Registry (NMLSR) or, in the case of an individual loan originator who is not a registered loan originator under the NMLSR, a criminal background check from a law enforcement agency or commercial service;

(B) A credit report from a consumer reporting agency described in section 603(p) of the Fair Credit Reporting Act (15 U.S.C. 1681a(p)) secured, where applicable, in compliance with the requirements of section 604(b) of the Fair Credit Reporting Act, 15 U.S.C. 1681b(b); and

(C) Information from the NMLSR about any administrative, civil, or criminal findings by any government jurisdiction or, in the case of an individual loan originator who is not a registered loan originator under the NMLSR, such information from the individual loan originator;

(ii) Determine on the basis of the information obtained pursuant to paragraph (f)(3)(i) of this section and any other information reasonably available to the loan originator organization, for any individual whom the loan originator organization hired on or after January 1, 2014 (or whom the loan originator organization hired before this date but for whom there were no applicable statutory or regulatory background standards in effect at the time of hire or before January 1, 2014, used to screen the individual) and for any individual regardless of when hired who, based on reliable information known to the loan originator organization, likely does not meet the standards under this paragraph (f)(3)(ii), before the individual acts as a loan originator in a consumer credit transaction secured by a dwelling, that the individual loan originator:

(A)

(1) Has not been convicted of, or pleaded guilty or nolo contendere to, a felony in a domestic or military court during the preceding seven-year period or, in the case of a felony involving an act of fraud, dishonesty, a breach of trust, or money laundering, at any time;

(2) For purposes of this paragraph (f)(3)(ii)(A):

(i) A crime is a felony only if at the time of conviction it was classified as a felony under the law of the jurisdiction under which the individual was convicted;

(ii) Expunged convictions and pardoned convictions do not render an individual unqualified; and

(iii) A conviction or plea of guilty or nolo contendere does not render an individual unqualified under this §1026.36(f) if the loan originator organization has obtained consent to employ the individual from the Federal Deposit Insurance Corporation (or the Board of Governors of the Federal Reserve System, as applicable) pursuant to section 19 of the Federal Deposit Insurance Act (FDIA), 12 U.S.C. 1829, the National Credit Union Administration pursuant to section 205 of the Federal Credit Union Act (FCUA), 12 U.S.C. 1785(d), or the Farm Credit Administration pursuant to section 5.65(d) of the Farm Credit Act of 1971 (FCA), 12 U.S.C. 227a-14(d), notwithstanding the bars posed with respect to that conviction or plea by the FDIA, FCUA, and FCA, as applicable; and

(B) Has demonstrated financial responsibility, character, and general fitness such as to warrant a determination that the individual loan originator will operate honestly, fairly, and efficiently; and

(iii) Provide periodic training covering Federal and State law requirements that apply to the individual loan originator's loan origination activities.

Regulatory Commentary

[Omitted.]

Section 7: Name and NMLSR ID
12 C.F.R. § 1026.36(g)

Name and NMLSR ID on Loan Documents - 12 CFR § 1026.36(g)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) For a consumer credit transaction secured by a dwelling, a loan originator organization must include on the loan documents described in paragraph (g)(2) of this section, whenever each such loan document is provided to a consumer or presented to a consumer for signature, as applicable:

(i) Its name and NMLSR ID, if the NMLSR has provided it an NMLSR ID; and

(ii) The name of the individual loan originator (as the name appears in the NMLSR) with primary responsibility for the origination and, if the NMLSR has provided such person an NMLSR ID, that NMLSR ID.

(2) The loan documents that must include the names and NMLSR IDs pursuant to paragraph (g)(1) of this section are:

(i) The credit application;

(ii) The disclosures required by §1026.19 (e) and (f);

(iii) The note or loan contract; and

(iv) The security instrument.

(3) For purposes of this section, 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 public access to the employment history of, and the publicly adjudicated disciplinary and enforcement actions against, loan originators.

Regulatory Commentary

[Omitted.]

Section 8: Prohibition: Arbitration and Waivers
12 C.F.R. § 1026.36(h)

Prohibition on Mandatory Arbitration Clauses and Waivers of Certain Consumer Rights - 12 CFR § 1026.36(h)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) **Arbitration.** 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) may not include terms that require arbitration or any other non-judicial procedure to resolve any controversy or settle any claims arising out of the transaction. This prohibition does not limit a consumer and creditor or any assignee from agreeing, after a dispute or claim under the transaction arises, to settle or use arbitration or other non-judicial procedure to resolve that dispute or claim.

(2) **No waivers of Federal statutory causes of action.** A contract or other agreement relating to a consumer credit transaction secured by a dwelling (including a home equity line of credit secured by the consumer's principal dwelling) may not be 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. This prohibition does not limit a consumer and creditor or any assignee from agreeing, after a dispute or claim under the transaction arises, to settle or use arbitration or other non-judicial procedure to resolve that dispute or claim.

Regulatory Commentary

None.

Section 9: Prohibition on Financing Credit Insurance

12 C.F.R. § 1026.36(i)

Prohibition on Financing Credit Insurance - 12 CFR § 1026.36(i)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) 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). This prohibition does not apply to credit insurance for which premiums or fees are calculated and paid in full on a monthly basis.

(2) For purposes of this paragraph (i):

(i) "Credit insurance":

(A) Means credit life, credit disability, credit unemployment, or credit property insurance, or any other accident, loss-of-income, life, or health insurance, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract, but

(B) Excludes credit unemployment insurance for which 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;

(ii) A creditor finances premiums or fees for credit insurance if it provides a consumer the right to defer payment of a credit insurance premium or fee owed by the consumer beyond the monthly period in which the premium or fee is due; and

(iii) Credit insurance premiums or fees are calculated on a monthly basis if they are determined mathematically by multiplying a rate by the actual monthly outstanding balance.

Regulatory Commentary

[Omitted.]

Section 10: Policies and Procedures
12 C.F.R. § 1026.36(j)

Policies and Procedures to Ensure and Monitor Compliance - 12 CFR § 1026.36(j)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) 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 of paragraphs (d), (e), (f), and (g) of this section. 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.

(2) For purposes of this paragraph (j), “depository institution” has the meaning in section 1503(3) of the SAFE Act, 12 U.S.C. 5102(3). For purposes of this paragraph (j), “subsidiary” has the meaning in section 3 of the Federal Deposit Insurance Act, 12 U.S.C. 1813.

Regulatory Commentary

None.

Section 11: Negative Amortization Counseling
12 C.F.R. § 1026.36(k)

Negative Amortization Counseling – 12 CFR 1026.36(k)

Regulatory Discussion

We have elected to not offer a Regulatory Discussion of this section.

Regulatory Text

(1) **Counseling required.** A creditor shall not extend credit to a first-time borrower in connection with a closed-end transaction secured by a dwelling, other than a reverse mortgage transaction subject to §1026.33 or a transaction secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53D), that may result in negative amortization, unless the creditor receives documentation that the consumer has obtained homeownership counseling from a counseling organization or counselor certified or approved by the U.S. Department of Housing and Urban Development to provide such counseling.

(2) **Definitions.** For the purposes of this paragraph (k), the following definitions apply:

(i) A **"first-time borrower"** means a consumer who has not previously received a closed-end credit transaction or open-end credit plan secured by a dwelling.

(ii) **"Negative amortization"** means a payment schedule with regular periodic payments that cause the principal balance to increase.

(3) **Steering prohibited.** A creditor that extends credit to a first-time borrower in connection with a closed-end transaction secured by a dwelling, other than a reverse mortgage transaction subject to §1026.33 or a transaction secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53D), that may result in negative amortization shall not steer or otherwise direct a consumer to choose a particular counselor or counseling organization for the counseling required under this paragraph (k).

Regulatory Commentary

[Omitted.]

Periodic Statements for Residential Mortgage Loans

Section 1: In General
12 C.F.R. § 1026.41(a)

In General - 12 C.F.R § 1026.41(a)

Regulatory Discussion

This section, in general, applies to a closed-end consumer credit transaction secured by a dwelling; and is referred to as a *mortgage loan* for purposes of this section.

- A servicer (i.e., the creditor, assignee, or servicer, as applicable) of
- a *mortgage loan* (i.e., a closed-end consumer credit transaction secured by a dwelling)
- shall provide a periodic statement for each billing cycle.

The commentary provides additional information on the following topics: Recipient of periodic statement; Billing cycles shorter than a 31-day period; One statement per billing cycle; and Opting out.

Exemptions to the periodic statement requirements are discussed in Section 5, below.

Regulatory Text

(a) **In general**

(1) **Scope.** This section applies to a closed-end consumer credit transaction secured by a dwelling, unless an exemption in paragraph (e) of this section applies. A closed-end consumer credit transaction secured by a dwelling is referred to as a *mortgage loan* for purposes of this section.

(2) **Periodic statements.** A servicer of a transaction subject to this section shall provide the consumer, for each billing cycle, a periodic statement meeting the requirements of paragraphs (b), (c), and (d) of this section. If a mortgage loan has a billing cycle shorter than a period of 31 days (for example, a bi-weekly billing cycle), a periodic statement covering an entire month may be used. For the purposes of this section, *servicer* includes the creditor, assignee, or servicer, as applicable. A creditor or assignee that does not currently own the mortgage loan or the mortgage servicing rights is not subject to the requirement in this section to provide a periodic statement.

Regulatory Commentary

41(a) In general.

1. ***Recipient of periodic statement.*** *When two consumers are joint obligors with primary liability on a closed-end consumer credit transaction secured by a dwelling, subject to*

§1026.41, the periodic statement may be sent to either one of them. For example, if a husband and wife jointly own a home, the servicer need not send statements to both the husband and the wife; a single statement may be sent.

2. ***Billing cycles shorter than a 31-day period.*** *If a loan has a billing cycle shorter than a period of 31 days (for example, a bi-weekly billing cycle), a periodic statement covering an entire month may be used. Such statement would separately list the upcoming payment due dates and amounts due, as required by §1026.20(d)(1), and list all transaction activity that occurred during the related time period, as required by paragraph (d)(4). Such statement may aggregate the information for the explanation of amount due, as required by paragraph (d)(2), and past payment breakdown, as required by paragraph (d)(3).*

3. ***One statement per billing cycle.*** *The periodic statement requirement in §1026.41 applies to the "creditor, assignee, or servicer as applicable." The creditor, assignee, and servicer are all subject to this requirement (but see comment 41(a)-4), but only one statement must be sent to the consumer each billing cycle. When two or more parties are subject to this requirement, they may decide among themselves which of them will send the statement.*

4. ***Opting out.*** *A consumer may not opt out of receiving periodic statements altogether. However, consumers who have demonstrated the ability to access statements online may opt out of receiving notifications that statements are available. Such an ability may be demonstrated, for example, by the consumer receiving notification that the statements is available, going to the Web site where the information is available, viewing the information about their account and selecting a link or option there to indicate they no longer would like to receive notifications when new statements are available.*

Section 2: Timing of the Periodic Statement
12 C.F.R. § 1026.41(b)

Timing of the Periodic Statements - 12 C.F.R § 1026.41(b)

Regulatory Discussion

The periodic payment must be delivered or mailed:

- within a reasonably prompt time (i.e., within four days of the close of the "courtesy period" of the previous billing cycle)
- after the payment due date or the end of any "courtesy period" provided for the previous billing cycle.

Regulatory Text

(b) **Timing of the periodic statement.** 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.

Regulatory Commentary

41(b) Timing of the periodic statement.

1. ***Reasonably prompt time.*** *Section 1026.41(b) requires that the periodic statement be delivered or placed in the mail no later than a reasonably prompt time after the payment due date or the end of any courtesy period. Delivering, emailing or placing the periodic statement in the mail within four days of the close of the courtesy period of the previous billing cycle generally would be considered reasonably prompt.*
2. ***Courtesy period.*** *The meaning of "courtesy period" is explained in comment 7(b)(11)-1.*

Section 3: Form of the Periodic Statement 12 C.F.R. § 1026.41(c)

Form of the Periodic Statement - 12 C.F.R § 1026.41(c)

Regulatory Discussion

The periodic statement must:

- be clear and conspicuous;
- in writing (or electronically if the consumer agrees); and
- in a form the consumer may keep

See the commentary for additional information on the following topics: *Clear and conspicuous standard; Additional information; disclosures required by other laws; Electronic distribution; and Presumed consent.*

Regulatory Text

(c) **Form of the periodic statement**. The servicer must make the disclosures required by this section clearly and conspicuously in writing, or electronically if the consumer agrees, and in a form that the consumer may keep. Sample forms for periodic statements are provided in appendix H-30. Proper use of these forms complies with the requirements of this paragraph (c) and the layout requirements in paragraph (d) of this section.

Regulatory Commentary

41(c) Form of the periodic statement.

1. ***Clear and conspicuous standard.*** *The "clear and conspicuous" standard generally requires that disclosures be in a reasonably understandable form. Except where otherwise provided, the standard does not prohibit adding to the required disclosures, as long as the additional information does not overwhelm or obscure the required disclosures. For example, while certain information about the escrow account (such as the account balance) is not required on the periodic statement, this information may be included.*

2. ***Additional information; disclosures required by other laws.*** *Nothing in §1026.41 prohibits a servicer from including additional information or combining disclosures required by other laws with the disclosures required by this subpart, unless such prohibition is expressly set forth in this subpart, or other applicable law.*

3. ***Electronic distribution.*** *The periodic statement may be provided electronically if the consumer agrees. The consumer must give affirmative consent to receive statements electronically. If statements are provided electronically, the creditor, assignee, or servicer* *may send a notification that a consumer's statement is available, with a link to where the statement can be accessed, in place of the statement itself.*

4. ***Presumed consent.*** *Any consumer who is currently receiving disclosures for any account (for example, a mortgage or checking account) electronically from their servicer shall be deemed to have consented to receiving e-statements in place of paper statements.*

Section 4: Content and Layout of the Periodic Statement

12 C.F.R. § 1026.41(d)

Form of the Periodic Statement - 12 C.F.R § 1026.41(d)

Regulatory Discussion

The periodic statement must include eight specific pieces of information as detailed in (d)(1) through (8), below.

The commentary provides additional information on the general *Content and layout of the periodic statement, as well as specific information on: the Past payment breakdown (d)(3); and Transaction Activity (d)(4).*

Regulatory Text

(d) **Content and layout of the periodic statement.** The periodic statement required by this section shall include:

(1) **Amount due.** Grouped together in close proximity to each other and located at the top of the first page of the statement:

(i) The payment due date;

(ii) The amount of any late payment fee, and the date on which that fee will be imposed if payment has not been received; and

(iii) The amount due, shown more prominently than other disclosures on the page and, if the transaction has multiple payment options, the amount due under each of the payment options.

(2) **Explanation of amount due.** The following items, grouped together in close proximity to each other and located on the first page of the statement:

(i) The monthly payment amount, including a breakdown showing how much, if any, will be applied to principal, interest, and escrow and, if a mortgage loan has multiple payment options, a breakdown of each of the payment options along with information on whether the principal balance will increase, decrease, or stay the same for each option listed;

(ii) The total sum of any fees or charges imposed since the last statement; and

(iii) Any payment amount past due.

(3) **Past Payment Breakdown**. The following items, grouped together in close proximity to each other and located on the first page of the statement:

(i) The total of all payments received since the last statement, including a breakdown showing the amount, if any, that was applied to principal, interest, escrow, fees and charges, and the amount, if any, sent to any suspense or unapplied funds account; and

(ii) The total of all payments received since the beginning of the current calendar year, including a breakdown of that total showing the amount, if any, that was applied to principal, interest, escrow, fees and charges, and the amount, if any, currently held in any suspense or unapplied funds account.

(4) **Transaction activity.** A list of all the transaction activity that occurred since the last statement. For purposes of this paragraph (d)(4), *transaction activity* means any activity that causes a credit or debit to the amount currently due. This list must include the date of the transaction, a brief description of the transaction, and the amount of the transaction for each activity on the list.

(5) **Partial payment information.** If a statement reflects a partial payment that was placed in a suspense or unapplied funds account, information explaining what must be done for the funds to be applied. The information must be on the front page of the statement or, alternatively, may be included on a separate page enclosed with the periodic statement or in a separate letter.

(6) **Contact information**. A toll-free telephone number and, if applicable, an electronic mailing address that may be used by the consumer to obtain information about the consumer's account, located on the front page of the statement.

(7) **Account information.** The following information:

(i) The amount of the outstanding principal balance;

(ii) The current interest rate in effect for the mortgage loan;

(iii) The date after which the interest rate may next change;

(iv) The existence of any prepayment penalty, as defined in §1026.32(b)(6)(i), that may be charged;

(v) The Web site to access either the Bureau list or the HUD list of homeownership counselors and counseling organizations and the HUD toll-free telephone number to access contact information for homeownership counselors or counseling organizations; and

(8) **Delinquency information.** If the consumer is more than 45 days delinquent, the following items, grouped together in close proximity to each other and located on the first page of the statement or, alternatively, on a separate page enclosed with the periodic statement or in a separate letter:

(i) The date on which the consumer became delinquent;

(ii) A notification of possible risks, such as foreclosure, and expenses, that may be incurred if the delinquency is not cured;

(iii) An account history showing, for the previous six months or the period since the last time the account was current, whichever is shorter, the amount remaining past due from each billing cycle or, if any such payment was fully paid, the date on which it was credited as fully paid;

(iv) A notice indicating any loss mitigation program to which the consumer has agreed, if applicable;

(v) A notice of whether the servicer has made the first notice or filing required by applicable law for any judicial or non-judicial foreclosure process, if applicable;

(vi) The total payment amount needed to bring the account current; and

(vii) A reference to the homeownership counselor information disclosed pursuant to paragraph (d)(7)(v) of this section.

Regulatory Commentary

41(d) Content and layout of the periodic statement.

1. ***Close proximity.*** *Paragraph (d) requires several disclosures to be provided in close proximity to one another. To meet this requirement, the items to be provided in close proximity must be grouped together, and set off from the other groupings of items. This could be accomplished in a variety of ways, for example, by presenting the information in boxes, or by arranging the items on the document and including spacing between the groupings. Items in close proximity may not have any intervening text between them.*
2. ***Not applicable.*** *If an item required by paragraph (d) or (e) of this section is not applicable to the loan, it may be omitted from the periodic statement or coupon book. For example, if there is no prepayment penalty associated with a loan, the prepayment penalty disclosures need not be provided on the periodic statement.*
3. ***Terminology.*** *A servicer may use terminology other than that found on the sample periodic statements in appendix H-30, so long as the new terminology is commonly understood. For example, servicers may take into consideration regional differences in terminology and refer to the account for the collection of taxes and insurance, referred to in §1026.41(d) as the "escrow account," as an "impound account."*

41(d)(3) Past payment breakdown.

1. ***Partial payments.*** *The disclosure of any partial payments received since the previous statement that were sent to a suspense or unapplied funds account as required by §1026.41(d)(3)(i) should reflect any funds that were received in the time period covered by the current statement and that were placed in such account. The disclosure of any portion of payments since the beginning of the calendar year that was sent to a partial payment or suspense account as required by §1026.41(d)(3)(ii) should reflect all funds that are*

currently held in a suspense or unapplied funds account. For example:

i. Suppose a payment of $1,000 is due, but the consumer sends in only $600 on January 1, which is held in a suspense account. Further assume there are no fees charged on this account. Assuming there are no other funds in the suspense account, the January statement should reflect: Unapplied funds since last statement—$600. Unapplied funds YTD—$600.

ii. Assume the same facts as in the preceding paragraph, except that during February the consumer sends in $300 and this too is held in the suspense account. The statement should reflect: Unapplied funds since last statement—$300. Unapplied funds YTD—$900.

iii. Assume the same facts as in the preceding paragraph, except that during March the consumer sends in $400. Of this payment, $100 completes a full periodic payment when added to the $900 in funds already held in the suspense account. This $1,000 is applied to the January payment, and the remaining $300 remains in the suspense account. The statement should reflect: Unapplied funds since last statement—$300. Unapplied Funds YTD—$300.

41(d)(4) Transaction Activity.

*1. **Meaning.** Transaction activity includes any transaction that credits or debits the amount currently due. This is the same amount that is required to be disclosed under §1026.41(d)(1)(iii). Examples of such transactions include, without limitation:*

i. Payments received and applied;

ii. Payments received and held in a suspense account;

iii. The imposition of any fees (for example late fees); and

iv. The imposition of any charges (for example, private mortgage insurance).

*2. **Description of late fees.** The description of any late fee charges includes the date of the late fee, the amount of the late fee, and the fact that a late fee was imposed.*

*3. **Partial payments.** If a partial payment is sent to a suspense or unapplied funds account, this fact must be in the transaction description along with the date and amount of the payment.*

H-30(A) Sample Form of Periodic Statement

Springside Mortgage

Customer Service: 1-800-555-1234
www.springsidemortgage.com

Mortgage Statement

Statement Date: 3/20/2012

Jordan and Dana Smith
4700 Jones Drive
Memphis, TN 38109

Account Number	**1234567**
Payment Due Date	**4/1/2012**
Amount Due	**$2,079.71**

If payment is received after 4/15/12, $160 late fee will be charged.

Account Information	
Outstanding Principal	$264,776.43
Interest Rate (Until October 2012)	4.75%
Prepayment Penalty	Yes

Explanation of Amount Due	
Principal	$386.46
Interest	$1,048.07
Escrow (for Taxes and Insurance)	$235.18
Regular Monthly Payment	**$1,669.71**
Total Fees Charged	$410.00
Total Amount Due	**$2,079.71**

Transaction Activity (2/21 to 3/20)

Date	Description	Charges	Payments
3/16/12	Late Fee (charged because full payment not received by 3/15/2012)	$160.00	
3/17/12	Payment Received – Thank you		$1,669.71
3/19/12	Property Inspection Fee	$250.00	

Past Payments Breakdown

	Paid Last Month	Paid Year to Date
Principal	$384.93	$1,150.25
Interest	$1,049.60	$3,153.34
Escrow (Taxes and Insurance)	$235.18	$705.54
Fees	$0.00	$0.00
Total	$1,669.71	$5,009.13

H-30(B) Sample Form of Periodic Statement with Delinquency Box

Springside Mortgage
Customer Service: 1-800-555-1234
www.springsidemortgage.com

Mortgage Statement
Statement Date: 3/20/2012

Jordan and Dana Smith
4700 Jones Drive
Memphis, TN 38109

Account Number	**1234567**
Payment Due Date	**4/1/2012**
Amount Due	**$4,339.13**

If payment is received after 4/15/12, $160 late fee will be charged.

Account Information	
Outstanding Principal	$264,776.43
Interest Rate (Until October 2012)	4.75%
Prepayment Penalty	Yes

Explanation of Amount Due	
Principal	$386.46
Interest	$1,048.07
Escrow (Taxes and Insurance)	$235.18
Regular Monthly Payment	**$1,669.71**
Total Fees and Charges	$410.00
Overdue Payment	$2,259.42
Total Amount Due	**$4,339.13**

Transaction Activity (2/20 to 3/19)

Date	Description	Charges	Payments
3/13/12	Partial Payment Received*		$1,000.00
3/16/12	Late Fee (charged because full payment not received by 3/15/2012)	$160.00	
3/19/12	Property Inspection Fee	$250.00	

Past Payments Breakdown

	Paid Last Month	Paid Year to Date
Principal	$0.00	$383.31
Interest	$0.00	$1,051.22
Escrow (Taxes and Insurance)	$0.00	$235.18
Fees	$0.00	$410.00
Partial Payment (Unapplied)*	$1,000.00	$1,490.00
Total	**$1,000.00**	**$3,569.71**

Important Messages

***Partial Payments:** Any partial payments that you make are not applied to your mortgage, but instead are held in a separate suspense account. If you pay the balance of a partial payment, the funds will then be applied to your mortgage.

****Delinquency Notice****

You are late on your mortgage payments. Failure to bring your loan current may result in fees and foreclosure—the loss of your home. As of March 20, you are 49 days delinquent on your mortgage loan.

Recent Account History

- Payment due 12/1/11: Fully paid on time
- Payment due 1/1/12: Fully paid on 2/3/12
- Payment due 2/1/12: Unpaid balance of $589.71
- Payment due 3/1/12: Unpaid balance of $2,079.71
- Current payment due 4/1/12: $1,669.71
- **Total: $4,339.13 due. You must pay this amount to bring your loan current.**

If You Are Experiencing Financial Difficulty: See back for information about mortgage counseling or assistance.

Springside Mortgage

Springside Mortgage
P.O. Box 11111
Los Angeles, CA 90010

Amount Due	
Due By 4/1/2012:	**$4,339.13**
$160 late fee will be charged after 4/15/12	
Additional Principal	$.
Additional Escrow	$.
Total Amount Enclosed	**$.**

Make check payable to Springside Mortgage.

Section 5: Exemptions
12 C.F.R. § 1026.41(e)

Exemptions - 12 C.F.R § 1026.41(e)

Regulatory Discussion

There are <u>*five exemptions*</u> to the periodic statement requirements for *mortgage loans* (i.e., a closed-end consumer credit transaction secured by a dwelling).

Exemptions (1) *Reverse mortgages*, (2) *Timeshare plans*, and (5) *Consumers in bankruptcy* are fairly straightforward.

Exemptions (3) *Coupon books* and (4) *Small servicers* are more complex; the commentary provides substantial information on these exemptions.

Regulatory Text

(e) **Exemptions**

(1) **Reverse mortgages.** Reverse mortgage transactions, as defined by §1026.33(a), are exempt from the requirements of this section.

(2) **Timeshare plans.** Transactions secured by consumers' interests in timeshare plans, as defined by 11 U.S.C. 101(53D), are exempt from the requirements of this section.

(3) **Coupon books.** The requirements of paragraph (a) of this section do not apply to fixed-rate loans if the servicer:

(i) Provides the consumer with a coupon book that includes on each coupon the information listed in paragraph (d)(1) of this section;

(ii) Provides the consumer with a coupon book that includes anywhere in the coupon book:

(A) The account information listed in paragraph (d)(7) of this section;

(B) The contact information for the servicer, listed in paragraph (d)(6) of this section; and

(C) Information on how the consumer can obtain the information listed in paragraph (e)(3)(iii) of this section;

(iii) Makes available upon request to the consumer by telephone, in writing, in person, or electronically, if the consumer consents, the information listed in paragraph (d)(2) through (5) of this section; and

(iv) Provides the consumer the information listed in paragraph (d)(8) of this section in writing, for any billing cycle during which the consumer is more than 45 days delinquent.

(4) **Small servicers**

(i) **Exemption.** A creditor, assignee, or servicer is exempt from the requirements of this section for mortgage loans serviced by a small servicer.

(ii) **Small servicer defined.** A small servicer is a servicer that:

(A) Services, together with any affiliates, 5,000 or fewer mortgage loans, for all of which the servicer (or an affiliate) is the creditor or assignee;

(B) Is a Housing Finance Agency, as defined in 24 CFR 266.5; or

(C) Is a nonprofit entity that services 5,000 or fewer mortgage loans, including any mortgage loans serviced on behalf of associated nonprofit entities, for all of which the servicer or an associated nonprofit entity is the creditor. For purposes of this paragraph (e)(4)(ii)(C), the following definitions apply:

(1) The term “nonprofit entity” means an entity having a tax exemption ruling or determination letter from the Internal Revenue Service under section 501(c)(3) of the Internal Revenue Code of 1986 (26 U.S.C. 501(c)(3); 26 CFR 1.501(c)(3)-1), and;

(2) The term “associated nonprofit entities” means nonprofit entities that by agreement operate using a common name, trademark, or servicemark to further and support a common charitable mission or purpose.

(iii) **Small servicer determination.** In determining whether a servicer satisfies paragraph (e)(4)(ii)(A) of this section, the servicer is evaluated based on the mortgage loans serviced by the servicer and any affiliates as of January 1 and for the remainder of the calendar year. In determining whether a servicer satisfies paragraph (e)(4)(ii)(C) of this section, the servicer is evaluated based on the mortgage loans serviced by the servicer as of January 1 and for the remainder of the calendar year. A servicer that ceases to qualify as a small servicer will have six months from the time it ceases to qualify or until the next January 1, whichever is later, to comply with any requirements from which the servicer is no longer exempt as a small servicer. The following mortgage loans are not considered in determining whether a servicer qualifies as a small servicer:

(A) Mortgage loans voluntarily serviced by the servicer for a creditor or assignee that is not an affiliate of the servicer and for which the servicer does not receive any compensation or fees.

(B) Reverse mortgage transactions.

(C) Mortgage loans secured by consumers' interests in timeshare plans.

(5) **Consumers in bankruptcy.** A servicer is exempt from the requirements of this section for a mortgage loan while the consumer is a debtor in bankruptcy under Title 11 of the United States Code.

Regulatory Commentary

41(e)(3) Coupon book exemption.

1. ***Fixed rate.*** *For guidance on the meaning of "fixed rate" for purposes of §1026.41(e)(3), see §1026.18(s)(7)(iii) and its commentary.*

2. ***Coupon book.*** *A coupon book is a booklet provided to the consumer with a page for each billing cycle during a set period of time (often covering one year). These pages are designed to be torn off and returned to the servicer with a payment for each billing cycle. Additional information about the loan is often included on or inside the front or back cover, or on filler pages in the coupon book.*

3. ***Information location.*** *The information required by paragraph (e)(3)(ii) need not be provided on each coupon, but should be provided somewhere in the coupon book. Such information could be located, e.g., on or inside the front or back cover, or on filler pages in the coupon book.*

4. ***Outstanding principal balance.*** *Paragraph (e)(3)(ii)(A) requires the information listed in paragraph (d)(7) to be included in the coupon book. Paragraph (d)(7)(i) requires the disclosure of the outstanding principal balance. If the servicer makes use of a coupon book and the exemption in §1026.41(e)(3), the servicer need only disclose the principal balance at the beginning of the time period covered by the coupon book.*

41(e)(4) Small servicers.

41(e)(4)(ii) Small servicer defined.

1. ***Mortgage loans considered.*** *Pursuant to §1026.41(a)(1), the mortgage loans considered in determining status as a small servicer are closed-end consumer credit transactions secured by a dwelling, subject to the exclusions in §1026.41(e)(4)(iii).*

2. ***Services, together with affiliates, 5,000 or fewer mortgage loans.*** *To qualify as a small servicer, under §1026.41(e)(4)(ii)(A), a servicer must service, together with any affiliates, 5,000 or fewer mortgage loans, for all of which the servicer (or an affiliate) is the creditor or assignee. There are two elements to satisfying §1026.41(e)(4)(ii)(A). First, a servicer, together with any affiliates, must service 5,000 or fewer mortgage loans. Second, a servicer must service only mortgage loans for which the servicer (or an affiliate) is the creditor or assignee. To be the creditor or assignee of a mortgage loan, the servicer (or an affiliate) must either currently own the mortgage loan or must have been the entity to which the mortgage loan obligation was initially payable (that is, the originator of the mortgage loan). A servicer is not a small servicer under §1026.41(e)(4)(ii)(A) if it services any mortgage loans for which the servicer or an affiliate is not the creditor or assignee (that is, for which the servicer or an affiliate is not the owner or was not the originator). The* *following two examples demonstrate circumstances in which a servicer would not qualify as a small servicer under §1026.41(e)(4)(ii)(A) because it did not meet both requirements under §1026.41(e)(4)(ii)(A) for determining a servicer's status as a small servicer:*

i. A servicer services 3,000 mortgage loans, all of which it or an affiliate owns or originated. An affiliate of the servicer services 4,000 other mortgage loans, all of which it or an affiliate owns or originated. Because the number of mortgage loans serviced by a servicer is determined by counting the mortgage loans serviced by a servicer together with any affiliates, both of these servicers are considered to be servicing 7,000 mortgage loans and neither servicer is a small servicer.

ii. A service services 3,100 mortgage loans—3,000 mortgage loans it owns or originated and 100 mortgage loans it neither owns nor originated, but for which it owns the mortgage servicing rights. The servicer is not a small servicer because it services mortgage loans for which the servicer (or an affiliate) is not the creditor or assignee, notwithstanding that the servicer services fewer than 5,000 mortgage loans.

*3. **Master servicing and subservicing.** A servicer that qualifies as a small servicer does not lose its small servicer status if it retains a subservicer, as that term is defined in 12 CFR 1024.31, to service any of its mortgage loans. A subservicer can gain the benefit of the small servicer exemption only if (1) the master servicer, as that term is defined in 12 CFR 1024.31, is a small servicer and (2) the subservicer is a small servicer. A subservicer generally will not qualify as a small servicer because it does not own or did not originate the mortgage loans it subservices—unless it is an affiliate of a master servicer that qualifies as a small servicer. The following examples demonstrate the application of the small servicer exemption for different forms of servicing relationships:*

i. A credit union services 4,000 mortgage loans, all of which it originated or owns. The credit union retains a credit union service organization, that is not an affiliate, to subservice 1,000 of the mortgage loans. The credit union is a small servicer and, thus, can gain the benefit of the small servicer exemption for the 3,000 mortgage loans the credit union services itself. The credit union service organization is not a small servicer because it services mortgage loans it does not own or did not originate. Accordingly, the credit union service organization does not gain the benefit of the small servicer exemption and, thus, must comply with any applicable mortgage servicing requirements for the 1,000 mortgage loans it subservices.

ii. A bank holding company, through a lender subsidiary, owns or originated 4,000 mortgage loans. All mortgage servicing rights for the 4,000 mortgage loans are owned by a wholly owned master servicer subsidiary. Servicing for the 4,000 mortgage loans is conducted by a wholly owned subservicer subsidiary. The bank holding company controls all of these subsidiaries and, thus, they are affiliates of the bank holding company pursuant 12 CFR 1026.32(b)(2). Because the master servicer and subservicer service 5,000 or fewer mortgage loans, and because all the mortgage loans are owned or originated by an affiliate, the master servicer and the subservicer both qualify for the small servicer exemption for all 4,000 mortgage loans.

iii. A nonbank servicer services 4,000 mortgage loans, all of which it originated or owns. The servicer retains a "component servicer" to assist it with servicing functions. The component servicer is not engaged in "servicing" as defined in 12 CFR 1024.2; that is, *the component servicer does not receive any scheduled periodic payments from a borrower pursuant to the terms of any mortgage loan, including amounts for escrow accounts, and does not make the payments to the owner of the loan or other third parties of principal and interest and such other payments with respect to the amounts received from the borrower as may be required pursuant to the terms of the mortgage servicing loan documents or servicing contract. The component servicer is not a subservicer pursuant to 12 CFR 1024.31 because it is not engaged in servicing, as that term is defined in 12 CFR 1024.2. The nonbank servicer is a small servicer and, thus, can gain the benefit of the small servicer exemption with regard to all 4,000 mortgage loans it services.*

4. ***Nonprofit entity that services 5,000 or fewer mortgage loans.*** *To qualify as a small servicer under §1026.41(e)(4)(ii)(C), a servicer must be a nonprofit entity that services 5,000 or fewer mortgage loans, including any mortgage loans serviced on behalf of associated nonprofit entities, for all of which the servicer or an associated nonprofit entity is the creditor. There are two elements to satisfying §1026.41(e)(4)(ii)(C). First, a nonprofit entity must service 5,000 or fewer mortgage loans, including any mortgage loans serviced on behalf of associated nonprofit entities. For each associated nonprofit entity, the small servicer determination is made separately, without consideration of the number of loans serviced by another associated nonprofit entity. Second, a nonprofit entity must service only mortgage loans for which the servicer (or an associated nonprofit entity) is the creditor. To be the creditor, the servicer (or an associated nonprofit entity) must have been the entity to which the mortgage loan obligation was initially payable (that is, the originator of the mortgage loan). A nonprofit entity is not a small servicer under §1026.41(e)(4)(ii)(C) if it services any mortgage loans for which the servicer (or an associated nonprofit entity) is not the creditor (that is, for which the servicer or an associated nonprofit entity was not the originator). The first of the following two examples demonstrates circumstances in which a nonprofit entity would qualify as a small servicer under §1026.41(e)(4)(ii)(C) because it meets both requirements for determining a nonprofit entity's status as a small servicer under §1026.41(e)(4)(ii)(C). The second example demonstrates circumstances in which a nonprofit entity would not qualify as a small servicer under §1026.41(e)(4)(ii)(C) because it does not meet both requirements under §1026.41(e)(4)(ii)(C).*

   i. Nonprofit entity A services 3,000 of its own mortgage loans, and 1,500 mortgage loans on behalf of associated nonprofit entity B. All 4,500 mortgage loans were originated by A or B. Associated nonprofit entity C services 2,500 mortgage loans, all of which it originated. Because the number of mortgage loans serviced by a nonprofit entity is determined by counting the number of mortgage loans serviced by the nonprofit entity (including mortgage loans serviced on behalf of associated nonprofit entities) but not counting any mortgage loans serviced by an associated nonprofit entity, A and C are both small servicers.

   ii. A nonprofit entity services 4,500 mortgage loans—3,000 mortgage loans it originated, 1,000 mortgage loans originated by associated nonprofit entities, and 500 mortgage loans neither it nor an associated nonprofit entity originated. The nonprofit entity is not a small servicer because it services mortgage loans for which neither it nor an associated nonprofit entity is the creditor, notwithstanding that it services fewer than 5,000 mortgage loans.

41(e)(4)(iii) Small servicer determination.

*1. **Loans obtained by merger or acquisition.** Any mortgage loans obtained by a servicer or an affiliate as part of a merger or acquisition, or as part of the acquisition of all of the assets or liabilities of a branch office of a creditor, should be considered mortgage loans for which the servicer or an affiliate is the creditor to which the mortgage loan is initially payable. A branch office means either an office of a depository institution that is approved as a branch by a Federal or State supervisory agency or an office of a for-profit mortgage lending institution (other than a depository institution) that takes applications from the public for mortgage loans.*

*2. **Timing for small servicer exemption.** The following examples demonstrate when a servicer either is considered or is no longer considered a small servicer under §1026.41(e)(4)(ii)(A) and (C):*

i. Assume a servicer (that as of January 1 of the current year qualifies as a small servicer) begins servicing more than 5,000 mortgage loans on October 1, and services more than 5,000 mortgage loans as of January 1 of the following year. The servicer would no longer be considered a small servicer on January 1 of the following year and would have to comply with any requirements from which it is no longer exempt as a small servicer on April 1 of the following year.

ii. Assume a servicer (that as of January 1 of the current year qualifies as a small servicer) begins servicing more than 5,000 mortgage loans on February 1, and services more than 5,000 mortgage loans as of January 1 of the following year. The servicer would no longer be considered a small servicer on January 1 of the following year and would have to comply with any requirements from which it is no longer exempt as a small servicer on that same January 1.

iii. Assume a servicer (that as of January 1 of the current year qualifies as a small servicer) begins servicing more than 5,000 mortgage loans on February 1, but services fewer than 5,000 mortgage loans as of January 1 of the following year. The servicer is considered a small servicer for the following year.

*3. **Mortgage loans not considered in determining whether a servicer is a small servicer.** Mortgage loans that are not considered pursuant to §1026.41(e)(4)(iii) in applying §1026.41(e)(4)(ii)(A) are not considered either for determining whether a servicer (together with any affiliates) services 5,000 or fewer mortgage loans or whether a servicer is servicing only mortgage loans that it (or an affiliate) owns or originated. For example, assume a servicer services 5,400 mortgage loans. Of these mortgage loans, the servicer owns or originated 4,800 mortgage loans, voluntarily services 300 mortgage loans that neither it (nor an affiliate) owns or originated and for which the servicer does not receive any compensation or fees, and services 300 reverse mortgage transactions. The voluntarily serviced mortgage loans and reverse mortgage loans are not considered in determining whether the servicer qualifies as a small servicer pursuant to §1026.41(e)(4)(iii)(A). Thus, because only the 4,800 mortgage loans owned or originated by the servicer are considered in determining whether the servicer qualifies as a small servicer, the servicer satisfies §1026.41(e)(4)(ii)(A) with regard to all 5,400 mortgage loans it services.*

4. ***Mortgage loans not considered in determining whether a nonprofit entity is a small servicer.*** *Mortgage loans that are not considered pursuant to §1026.41(e)(4)(iii) in applying §1026.41(e)(4)(ii)(C) are not considered either for determining whether a nonprofit entity services 5,000 or fewer mortgage loans, including any mortgage loans serviced on behalf of associated nonprofit entities, or whether a nonprofit entity is servicing only mortgage loans that it or an associated nonprofit entity originated. For example, assume a servicer that is a nonprofit entity services 5,400 mortgage loans. Of these mortgage loans, the nonprofit entity originated 2,800 mortgage loans and associated nonprofit entities originated 2,000 mortgage loans. The nonprofit entity receives compensation for servicing the loans originated by associated nonprofits. The nonprofit entity also voluntarily services 600 mortgage loans that were originated by an entity that is not an associated nonprofit entity, and receives no compensation or fees for servicing these loans. The voluntarily serviced mortgage loans are not considered in determining whether the servicer qualifies as a small servicer. Thus, because only the 4,800 mortgage loans originated by the nonprofit entity or associated nonprofit entities are considered in determining whether the servicer qualifies as a small servicer, the servicer satisfies §1026.41(e)(4)(ii)(C) with regard to all 5,400 mortgage loans it services.*

5. ***Limited role of voluntarily serviced mortgage loans.*** *Reverse mortgages and mortgage loans secured by consumers' interests in timeshare plans, in addition to not being considered in determining small servicer qualification, are also exempt from the requirements of §1026.41. In contrast, although voluntarily serviced mortgage loans, as defined by §1026.41(e)(4)(iii)(A), are likewise not considered in determining small servicer status, they are not exempt from the requirements of §1026.41. Thus, a servicer that does not qualify as a small servicer would not have to provide periodic statements for reverse mortgages and timeshare plans because they are exempt from the rule, but would have to provide periodic statements for mortgage loans it voluntarily services.*

41(e)(5) Consumers in bankruptcy.

1. ***Commencing a case.*** *The requirements of §1026.41 do not apply once a petition is filed under Title 11 of the United States Code, commencing a case in which the consumer is a debtor.*

2. ***Obligation to resume sending periodic statements.***

   i. *With respect to any portion of the mortgage debt that is not discharged, a servicer must resume sending periodic statements in compliance with §1026.41 within a reasonably prompt time after the next payment due date that follows the earliest of any of three potential outcomes in the consumer's bankruptcy case: the case is dismissed, the case is closed, or the consumer receives a discharge under 11 U.S.C. 727, 1141, 1228, or 1328. However, this requirement to resume sending periodic statements does not require a servicer to communicate with a consumer in a manner that would be inconsistent with applicable bankruptcy law or a court order in a bankruptcy case. To the extent permitted by such law or court order, a servicer may adapt the requirements of §1026.41 in any manner believed necessary.*

   ii. *The periodic statement is not required for any portion of the mortgage debt that is discharged under applicable provisions of the U.S. Bankruptcy Code. If the consumer's* *bankruptcy case is revived—for example if the court reinstates a previously dismissed case, reopens the case, or revokes a discharge—the servicer is again exempt from the requirement in §1026.41.*

3. ***Joint obligors.*** *When two or more consumers are joint obligors with primary liability on a closed-end consumer credit transaction secured by a dwelling subject to §1026.41, the exemption in §1026.41(e)(5) applies if any of the consumers is in bankruptcy. For example, if a husband and wife jointly own a home, and the husband files for bankruptcy, the servicer is exempt from providing periodic statements to both the husband and the wife.*

Valuation Independence

Section 1: Scope and Definitions
12 C.F.R. § 1026.42(a) and 12 C.F.R. § 1026.42(b)

Scope - 12 CFR § 1026.42(a)

Regulatory Discussion

The scope of this section applies to any (either open- or closed-end) consumer credit transaction that is secured by the consumer's principal dwelling.

Regulatory Text

(a) **Scope.** This section applies to any consumer credit transaction secured by the consumer's principal dwelling.

Regulatory Commentary

42(a) Scope

*1. **Open- and closed-end credit.** Section 1026.42 applies to both open-end and closed-end transactions secured by the consumer's principal dwelling.*

*2. **Consumer's principal dwelling.** Section 1026.42 applies only if the dwelling that will secure a consumer credit transaction is the principal dwelling of the consumer who obtains credit.*

Definitions - 12 CFR § 1026.42(b)

Regulatory Discussion

There are four terms, specific to this section, with the following definitions.

The Commentary also makes reference to the definition of "principal dwelling."

Regulatory Text

(b) **Definitions.** For purposes of this section:

(1) **"Covered person"** means a creditor with respect to a covered transaction or a person

that provides "settlement services," as defined in 12 U.S.C. 2602(3) and implementing regulations, in connection with a covered transaction.

(2) **"Covered transaction"** means an extension of consumer credit that is or will be secured by the consumer's principal dwelling, as defined in §1026.2(a)(19).

(3) **"Valuation"** means an estimate of the value of the consumer's principal dwelling in written or electronic form, other than one produced solely by an automated model or system.

(4) **"Valuation management functions"** means:

(i) Recruiting, selecting, or retaining a person to prepare a valuation;

(ii) Contracting with or employing a person to prepare a valuation;

(iii) Managing or overseeing the process of preparing a valuation, including by providing administrative services such as receiving orders for and receiving a valuation, submitting a completed valuation to creditors and underwriters, collecting fees from creditors and underwriters for services provided in connection with a valuation, and compensating a person that prepares valuations; or

(iv) Reviewing or verifying the work of a person that prepares valuations.

Regulatory Commentary

42(b) Definitions

Paragraph 42(b)(1)

*1. **Examples of covered persons.** "Covered persons" include creditors, mortgage brokers, appraisers, appraisal management companies, real estate agents, and other persons that provide "settlement services" as defined under the Real Estate Settlement Procedures Act and implementing regulations. See 12 U.S.C. 2602(3).*

*2. **Examples of persons not covered.** The following persons are not "covered persons" (unless, of course, they are creditors with respect to a covered transaction or perform "settlement services" in connection with a covered transaction):*

i. The consumer who obtains credit through a covered transaction.

ii. A person secondarily liable for a covered transaction, such as a guarantor.

iii. A person that resides in or will reside in the consumer's principal dwelling but will not be liable on the covered transaction, such as a non-obligor spouse.

Paragraph 42(b)(2)

*1. **Principal dwelling.** The term "principal dwelling" has the same meaning under §1026.42(b) as under §§1026.2(a)(24), 1026.15(a), and 1026.23(a). See comments 2(a)(24)-3, 15(a)-5, and 23(a)-3.*

Paragraph 42(b)(3)

1. ***Valuation.*** *A "valuation" is an estimate of value prepared by a natural person, such as an appraisal report prepared by an appraiser or an estimate of market value prepared by a real estate agent. The term includes photographic or other information included with a written estimate of value. A "valuation" includes an estimate provided or viewed electronically, such as an estimate transmitted via electronic mail or viewed using a computer.*

2. ***Automated model or system.*** *A "valuation" does not include an estimate of value produced exclusively using an automated model or system. However, a "valuation" includes an estimate of value developed by a natural person based in part on an estimate of value produced using an automated model or system.*

3. ***Estimate.*** *An estimate of the value of the consumer's principal dwelling includes an estimate of a range of values for the consumer's principal dwelling.*

Section 2: Valuation of Principal Dwelling 12 C.F.R. § 1026.42(c)

Valuation of Principal Dwelling - 12 CFR § 1026.42(c)

Regulatory Discussion

This section begins with a discussion of the two prohibitions with respect to the valuation of a consumer's principal dwelling:

Coercion. No creditor (or person providing settlement services) shall (or attempt to) directly or indirectly cause the value of the dwelling to be based on any factor other than the independent judgment of a person that prepares valuations.

Mischaracterization of value. There are three components:

- Misrepresentation. No person that prepares valuations shall materially misrepresent the value of the dwelling.
- Falsification or alteration. No creditor (or person providing settlement services) shall falsify or materially alter a valuation.
- Inducement of mischaracterization. No creditor (or person providing settlement services) shall induce a person that prepares valuations to materially misrepresent the value of the dwelling.

Finally, this section provides six examples of actions that do not violate the prohibitions.

Regulatory Text

(c) **Valuation of consumer's principal dwelling**

(1) **Coercion.** In connection with a covered transaction, no covered person shall or shall attempt to directly or indirectly cause the value assigned to the consumer's principal dwelling to be based on any factor other than the independent judgment of a person that prepares valuations, through coercion, extortion, inducement, bribery, or intimidation of, compensation or instruction to, or collusion with a person that prepares valuations or performs valuation management functions.

(i) Examples of actions that violate paragraph (c)(1) include:

(A) Seeking to influence a person that prepares a valuation to report a minimum or maximum value for the consumer's principal dwelling;

(B) Withholding or threatening to withhold timely payment to a person that prepares a valuation or performs valuation management functions because the person does not value the consumer's principal dwelling at or above a certain amount;

(C) Implying to a person that prepares valuations that current or future retention of the person depends on the amount at which the person estimates the value of the consumer's principal dwelling;

(D) Excluding a person that prepares a valuation from consideration for future engagement because the person reports a value for the consumer's principal dwelling that does not meet or exceed a predetermined threshold; and

(E) Conditioning the compensation paid to a person that prepares a valuation on consummation of the covered transaction.

(2) **Mischaracterization of value**

(i) **Misrepresentation.** In connection with a covered transaction, no person that prepares valuations shall materially misrepresent the value of the consumer's principal dwelling in a valuation. A misrepresentation is material for purposes of this paragraph (c)(2)(i) if it is likely to significantly affect the value assigned to the consumer's principal dwelling. A *bona fide* error shall not be a misrepresentation.

(ii) **Falsification or alteration**. In connection with a covered transaction, no covered person shall falsify and no covered person other than a person that prepares valuations shall materially alter a valuation. An alteration is material for purposes of this paragraph (c)(2)(ii) if it is likely to significantly affect the value assigned to the consumer's principal dwelling.

(iii) **Inducement of mischaracterization.** In connection with a covered transaction, no covered person shall induce a person to violate paragraph (c)(2)(i) or (ii) of this section.

(3) **Permitted actions.** Examples of actions that do not violate paragraph (c)(1) or (c)(2) include:

(i) Asking a person that prepares a valuation to consider additional, appropriate property information, including information about comparable properties, to make or support a valuation;

(ii) Requesting that a person that prepares a valuation provide further detail, substantiation, or explanation for the person's conclusion about the value of the consumer's principal dwelling;

(iii) Asking a person that prepares a valuation to correct errors in the valuation;

(iv) Obtaining multiple valuations for the consumer's principal dwelling to select the most reliable valuation;

(v) Withholding compensation due to breach of contract or substandard performance of services; and

(vi) Taking action permitted or required by applicable Federal or state statute, regulation, or agency guidance.

Regulatory Commentary

42(c) Valuation for consumer's principal dwelling

42(c)(1) Coercion

1. ***State law.*** *The terms "coercion," "extortion," "inducement," "bribery," "intimidation," "compensation," "instruction," and "collusion" have the meanings given to them by applicable state law or contract. See §1026.2(b)(3).*

2. ***Purpose.*** *A covered person does not violate §1026.42(c)(1) if the person does not engage in an act or practice set forth in §1026.42(c)(1) for the purpose of causing the value assigned to the consumer's principal dwelling to be based on a factor other than the independent judgment of a person that prepares valuations. For example, requesting that a person that prepares a valuation take certain actions, such as consider additional, appropriate property information, does not violate §1026.42(c), because such request does not supplant the independent judgment of the person that prepares a valuation. See §1026.42(c)(3)(i). A covered person also may provide incentives, such as additional compensation, to a person that prepares valuations or performs valuation management functions under §1026.42(c)(1), as long as the covered person does not cause or attempt to cause the value assigned to the consumer's principal dwelling to be based on a factor other than the independent judgment of the person that prepares valuations.*

3. ***Person that prepares valuations.*** *For purposes of §1026.42, the term "valuation" includes an estimate of value regardless of whether it is an appraisal prepared by a state-certified or -licensed appraiser. See comment 42(b)(3)-1. A person that prepares valuations may or may not be a state-licensed or state-certified appraiser. Thus a person violates §1026.42(c)(1) by engaging in prohibited acts or practices directed towards any person that prepares or may prepare a valuation of the consumer's principal dwelling for a covered transaction. For example, a person violates §1026.42(c)(1) by seeking to coerce a real estate agent to assign a value to the consumer's principal dwelling based on a factor other than the independent judgment of the real estate agent, in connection with a covered transaction.*

4. ***Indirect acts or practices.*** *Section 1026.42(c)(1) prohibits both direct and indirect attempts to cause the value assigned to the consumer's principal dwelling to be based on a factor other than the independent judgment of the person that prepares the valuation, through coercion and certain other acts and practices. For example, a creditor violates §1026.42(c)(1) if the creditor attempts to cause the value an appraiser engaged by an appraisal management company assigns to the consumer's principal dwelling to be based on a factor other than the appraiser's independent judgment, by threatening to withhold future business from a title company affiliated with the appraisal management company unless the appraiser assigns a value to the dwelling that meets or exceeds a minimum threshold.*

Paragraph 42(c)(1)(i)

1. ***Applicability of examples.*** *Section 1026.42(c)(1)(i) provides examples of coercion of a person that prepares valuations. However, §1026.42(c)(1)(i) also applies to coercion of a person that performs valuation management functions or its affiliate. See §1026.42(c)(1); comment 42(c)(1) 4.*

2. ***Specific value or predetermined threshold.*** *As used in the examples of actions prohibited under §1026.42(c)(1), a "specific value" and a "predetermined threshold" include a predetermined minimum, maximum, or range of values. Further, although the examples assume a covered person's prohibited actions are designed to cause the value assigned to the consumer's principal dwelling to equal or exceed a certain amount, the rule applies equally to cases where a covered person's prohibited actions are designed to cause the value assigned to the dwelling to be below a certain amount.*

42(c)(2) Mischaracterization of Value

42(c)(2)(i) Misrepresentation

1. ***Opinion of value.*** *Section 1026.42(c)(2)(i) prohibits a person that performs valuations from misrepresenting the value of the consumer's principal dwelling in a valuation. Such person misrepresents the value of the consumer's principal dwelling by assigning a value to such dwelling that does not reflect the person's opinion of the value of such dwelling. For example, an appraiser misrepresents the value of the consumer's principal dwelling if the appraiser estimates that the value of such dwelling is $250,000 applying the standards required by the Uniform Standards of Professional Appraisal Standards but assigns a value of $300,000 to such dwelling in a Uniform Residential Appraisal Report.*

42(c)(2)(iii) Inducement of Mischaracterization

1. ***Inducement.*** *A covered person may not induce a person to materially misrepresent the value of the consumer's principal dwelling in a valuation or to falsify or alter a valuation. For example, a loan originator may not coerce a loan underwriter to alter an appraisal report to increase the value assigned to the consumer's principal dwelling.*

Section 3: Prohibition of Conflicts of Interest
12 C.F.R. § 1026.42(d)

In General - 12 CFR § 1026.42(d)(1)

Regulatory Discussion

With respect to a consumer credit transaction that is secured by the consumer's principal dwelling, this section generally *prohibits any person preparing a valuation* (or performing valuation management functions) *from having a direct or indirect interest* (financial or otherwise) *in the property or transaction*. Note: there are exceptions for employees and affiliate of the creditor and providers of multiple settlement services.

Regulatory Text

(d) **Prohibition on conflicts of interest**

(1)

(i) **In general.** No person preparing a valuation or performing valuation management functions for a covered transaction may have a direct or indirect interest, financial or otherwise, in the property or transaction for which the valuation is or will be performed.

(ii) **Employees and affiliates of creditors; providers of multiple settlement services.** In any covered transaction, no person violates paragraph (d)(1)(i) of this section based solely on the fact that the person:

(A) Is an employee or affiliate of the creditor; or

(B) Provides a settlement service in addition to preparing valuations or performing valuation management functions, or based solely on the fact that the person's affiliate performs another settlement service.

Regulatory Commentary

42(d)(1)(i) In General

*1. **Prohibited interest in the property.** A person preparing a valuation or performing valuation management functions for a covered transaction has a prohibited interest in the property under paragraph (d)(1)(i) if the person has any ownership or reasonably foreseeable ownership interest in the property. For example, a person who seeks a mortgage to purchase a home has a reasonably foreseeable ownership interest in the property* *securing the mortgage, and therefore is not permitted to prepare the valuation or perform valuation management functions for that mortgage transaction under paragraph (d)(1)(i).*

2. ***Prohibited interest in the transaction.*** *A person preparing a valuation or performing valuation management functions has a prohibited interest in the transaction under paragraph (d)(1)(i) if that person or an affiliate of that person also serves as a loan officer of the creditor, mortgage broker, real estate broker, or other settlement service provider for the transaction and the conditions under paragraph (d)(4) are not satisfied. A person also has a prohibited interest in the transaction if the person is compensated or otherwise receives financial or other benefits based on whether the transaction is consummated. Under these circumstances, the person is not permitted to prepare the valuation or perform valuation management functions for that transaction under paragraph (d)(1)(i).*

42(d)(1)(ii) Employees and Affiliates of Creditors; Providers of Multiple Settlement Services

1. ***Employees and affiliates of creditors.*** *In general, a creditor may use employees or affiliates to prepare a valuation or perform valuation management functions without violating paragraph (d)(1)(i). However, whether an employee or affiliate has a direct or indirect interest in the property or transaction that creates a prohibited conflict of interest under paragraph (d)(1)(i) depends on the facts and circumstances of a particular case, including the structure of the employment or affiliate relationship.*

2. ***Providers of multiple settlement services.*** *In general, a person who prepares a valuation or perform valuation management functions for a covered transaction may perform another settlement service for the same transaction, or the person's affiliate may perform another settlement service, without violating paragraph (d)(1)(i). However, whether the person has a direct or indirect interest in the property or transaction that creates a prohibited conflict of interest under paragraph (d)(1)(i) depends on the facts and circumstances of a particular case.*

Assets Exceed $250 Million - 12 CFR § 1026.42(d)(2)

Regulatory Discussion

This section discusses special rules for employees and affiliates of creditors with assets of more than $250 million (*<u>for both</u>* of the past two calendar years). *There is no violation of the general prohibition stated in (d)(1)(i), above, if <u>all three</u> conditions are met.*

Regulatory Text

(2) **Employees and affiliates of creditors with assets of more than $250 million for both of the past two calendar years.** For any covered transaction in which the creditor had assets of more than $250 million as of December 31st for both of the past

two calendar years, a person subject to paragraph (d)(1)(i) of this section who is employed by or affiliated with the creditor does not have a conflict of interest in violation of paragraph (d)(1)(i) of this section based on the person's employment or affiliate relationship with the creditor if:

(i) The compensation of the person preparing a valuation or performing valuation management functions is not based on the value arrived at in any valuation;

(ii) The person preparing a valuation or performing valuation management functions reports to a person who is not part of the creditor's loan production function, as defined in paragraph (d)(5)(i) of this section, and whose compensation is not based on the closing of the transaction to which the valuation relates; and

(iii) No employee, officer or director in the creditor's loan production function, as defined in paragraph (d)(5)(i) of this section, is directly or indirectly involved in selecting, retaining, recommending or influencing the selection of the person to prepare a valuation or perform valuation management functions, or to be included in or excluded from a list of approved persons who prepare valuations or perform valuation management functions.

Regulatory Commentary

42(d)(2) Employees and Affiliates of Creditors with Assets of More than $250 Million for Both of the Past two Calendar Years

1. ***Safe harbor.*** *A person who a prepares valuation or performs valuation management functions for a covered transaction and is an employee or affiliate of the creditor will not be deemed to have an interest prohibited under paragraph (d)(1)(i) on the basis of the employment or affiliate relationship with the creditor if the conditions in paragraph (d)(2) are satisfied. Even if the conditions in paragraph (d)(2) are satisfied, however, the person may have a prohibited conflict of interest on other grounds, such as if the person performs a valuation for a purchase-money mortgage transaction in which the person is the buyer or seller of the subject property. Thus, in general, in any covered transaction in which the creditor had assets of more than $250 million for both of the past two years, the creditor may use its own employee or affiliate to prepare a valuation or perform valuation management functions for a particular transaction, as long as the conditions described in paragraph (d)(2) are satisfied. If the conditions in paragraph (d)(2) are not satisfied, whether a person preparing a valuation or performing valuation management functions has violated paragraph (d)(1)(i) depends on all of the facts and circumstances.*

Paragraph 42(d)(2)(ii)

1. ***Prohibition on reporting to a person who is part of the creditor's loan production function.*** *To qualify for the safe harbor under paragraph (d)(2), the person preparing a valuation or performing valuation management functions may not report to a person who is part of the creditor's loan production function (as defined in paragraph (d)(5)(i) and comment 42(d)(5)(i)-1). For example, if a person preparing a valuation is directly supervised or managed by a loan officer or other person in the creditor's loan production function, or by a person who*

is directly supervised or managed by a loan officer, the condition under paragraph (d)(2)(ii) is not met.

2. ***Prohibition on reporting to a person whose compensation is based on the transaction closing.*** *To qualify for the safe harbor under paragraph (d)(2), the person preparing a valuation or performing valuation management functions may not report to a person whose compensation is based on the closing of the transaction to which the valuation relates. For example, assume an appraisal management company performs valuation management functions for a transaction in which the creditor is an affiliate of the appraisal management company. If the employee of the appraisal management company who is in charge of valuation management functions for that transaction is supervised by a person who earns a commission or bonus based on the percentage of closed transactions for which the appraisal management company provides valuation management functions, the condition under paragraph (d)(2)(ii) is not met.*

Paragraph 42(d)(2)(iii)

1. ***Direct or indirect involvement in selection of person who prepares a valuation.*** *In any covered transaction, the safe harbor under paragraph (d)(2) is available if, among other things, no employee, officer or director in the creditor's loan production function (as defined in paragraph (d)(4)(ii) and comment 42(d)(4)(ii)-1) is directly or indirectly involved in selecting, retaining, recommending or influencing the selection of the person to prepare a valuation or perform valuation management functions, or to be included in or excluded from a list or panel of approved persons who prepare valuations or perform valuation management functions. For example, if the person who selects the person to prepare the valuation for a covered transaction is supervised by an employee of the creditor who also supervises loan officers, the condition in paragraph (d)(2)(iii) is not met.*

Assets Less Than $250 Million - 12 CFR § 1026.42(d)(3)

Regulatory Discussion

This section discusses special rules for employees and affiliates of creditors with assets of $250 million or less (<u>*for either*</u> of the past two calendar years). *There is no violation of the general prohibition stated in (d)(1)(i), above, if* <u>*both of two*</u> *conditions are met.*

Regulatory Text

(3) **Employees and affiliates of creditors with assets of $250 million or less for either of the past two calendar years.** For any covered transaction in which the creditor had assets of $250 million or less as of December 31st for either of the past two calendar years, a person subject to paragraph (d)(1)(i) of this section who is employed by or affiliated with the creditor does not have a conflict of interest in violation of paragraph (d)(1)(i) of this section based on the person's employment or

affiliate relationship with the creditor if:

(i) The compensation of the person preparing a valuation or performing valuation management functions is not based on the value arrived at in any valuation; and

(ii) The creditor requires that any employee, officer or director of the creditor who orders, performs, or reviews a valuation for a covered transaction abstain from participating in any decision to approve, not approve, or set the terms of that transaction.

Regulatory Commentary

42(d)(3) Employees and Affiliates of Creditors With Assets of $250 Million or Less for Either of the Past Two Calendar Years

*1. **Safe harbor.** A person who prepares a valuation or performs valuation management functions for a covered transaction and is an employee or affiliate of the creditor will not be deemed to have interest prohibited under paragraph (d)(1)(i) on the basis of the employment or affiliate relationship with the creditor if the conditions in paragraph (d)(3) are satisfied. Even if the conditions in paragraph (d)(3) are satisfied, however, the person may have a prohibited conflict of interest on other grounds, such as if the person performs a valuation for a purchase-money mortgage transaction in which the person is the buyer or seller of the subject property. Thus, in general, in any covered transaction in which the creditor had assets of $250 million or less for either of the past two calendar years, the creditor may use its own employee or affiliate to prepare a valuation or perform valuation management functions for a particular transaction, as long as the conditions described in paragraph (d)(3) are satisfied. If the conditions in paragraph (d)(3) are not satisfied, whether a person preparing valuations or performing valuation management functions has violated paragraph (d)(1)(i) depends on all of the facts and circumstances.*

Providers of Multiple Settlement Services - 12 CFR § 1026.42(d)(4)

Regulatory Discussion

This section discusses special rules for providers of multiple settlement services. There is no violation of the general prohibition stated in (d)(1)(i), above, if <u>either of two</u> conditions are met.

Regulatory Text

(4) **Providers of multiple settlement services.** For any covered transaction, a person who prepares a valuation or performs valuation management functions in addition to performing another settlement service for the transaction, or whose affiliate performs another settlement service for the transaction, does not have a conflict of interest in violation of paragraph (d)(1)(i) of this section as a result of the person or the person's

affiliate performing another settlement service for the transaction if:

(i) The creditor had assets of more than $250 million as of December 31st for both of the past two calendar years and the conditions in paragraph (d)(2)(i)-(iii) are met; or

(ii) The creditor had assets of $250 million or less as of December 31st for either of the past two calendar years and the conditions in paragraph (d)(3)(i)-(ii) are met.

Regulatory Commentary

42(d)(4) Providers of Multiple Settlement Services

Paragraph 42(d)(4)(i)

1. ***Safe harbor in transactions in which the creditor had assets of more than $250 million for both of the past two calendar years.*** *A person preparing a valuation or performing valuation management functions in addition to performing another settlement service for the same transaction, or whose affiliate performs another settlement service for the transaction, will not be deemed to have interest prohibited under paragraph (d)(1)(i) as a result of the person or the person's affiliate performing another settlement service if the conditions in paragraph (d)(4)(i) are satisfied. Even if the conditions in paragraph (d)(4)(i) are satisfied, however, the person may have a prohibited conflict of interest on other grounds, such as if the person performs a valuation for a purchase-money mortgage transaction in which the person is the buyer or seller of the subject property. Thus, in general, in any covered transaction with a creditor that had assets of more than $250 million for the past two years, a person preparing a valuation or performing valuation management functions, or its affiliate, may provide another settlement service for the same transaction, as long as the conditions described in paragraph (d)(4)(i) are satisfied. If the conditions in paragraph (d)(4)(i) are not satisfied, whether a person preparing valuations or performing valuation management functions has violated paragraph (d)(1)(i) depends on all of the facts and circumstances.*
2. ***Reporting.*** *The safe harbor under paragraph (d)(4)(i) is available if the condition specified in paragraph (d)(2)(ii), among others, is met. Paragraph (d)(2)(ii) prohibits a person preparing a valuation or performing valuation management functions from reporting to a person whose compensation is based on the closing of the transaction to which the valuation relates. For example, assume an appraisal management company performs both valuation management functions and title services, including providing title insurance, for the same covered transaction. If the appraisal management company employee in charge of valuation management functions for the transaction is supervised by the title insurance agent in the transaction, whose compensation depends in whole or in part on whether title insurance is sold at the loan closing, the condition in paragraph (d)(2)(ii) is not met.*

Paragraph 42(d)(4)(ii)

*1. **Safe harbor in transactions in which the creditor had assets of $250 million or less for either of the past two calendar years.** A person preparing a valuation or performing valuation management functions in addition to performing another settlement service for the same transaction, or whose affiliate performs another settlement service for the transaction, will not be deemed to have an interest prohibited under paragraph (d)(1)(i) as a result of the person or the person's affiliate performing another settlement service if the conditions in paragraph (d)(4)(ii) are satisfied. Even if the conditions in paragraph (d)(4)(ii) are satisfied, however, the person may have a prohibited conflict of interest on other grounds, such as if the person performs a valuation for a purchase-money mortgage transaction in which the person is the buyer or seller of the subject property. Thus, in general, in any covered transaction in which the creditor had assets of $250 million or less for either of the past two years, a person preparing a valuation or performing valuation management functions, or its affiliate, may provide other settlement services for the same transaction, as long as the conditions described in paragraph (d)(4)(ii) are satisfied. If the conditions in paragraph (d)(4)(ii) are not satisfied, whether a person preparing valuations or performing valuation management functions has violated paragraph (d)(1)(i) depends on all of the facts and circumstances.*

Definitions - 12 CFR § 1026.42(d)(5)

Regulatory Discussion

This section provides definitions of three terms specific to this paragraph (d).

Regulatory Text

(5) **Definitions.** For purposes of this paragraph (d), the following definitions apply:

(i) **Loan production function.** The term "loan production function" means an employee, officer, director, department, division, or other unit of a creditor with responsibility for generating covered transactions, approving covered transactions, or both.

(ii) **Settlement service.** The term "settlement service" has the same meaning as in the Real Estate Settlement Procedures Act, 12 U.S.C. 2601 *et seq.*

(iii) **Affiliate.** The term "affiliate" has the same meaning as in Regulation Y of the Board of Governors of the Federal Reserve System, 12 CFR 225.2(a).

Regulatory Commentary

42(d)(5)(i) Loan Production Function

*1. **Loan production function.** One condition of the safe harbors under paragraphs (d)(2) and (d)(4)(i), involving transactions in which the creditor had assets of more than $250* *million for both of the past two calendar years, is that the person who prepares a valuation or performs valuation management functions must report to a person who is not part of the creditor's "loan production function." A creditor's "loan production function" includes retail sales staff, loan officers, and any other employee of the creditor with responsibility for taking a loan application, offering or negotiating loan terms or whose compensation is based on loan processing volume. A person is not considered part of a creditor's loan production function solely because part of the person's compensation includes a general bonus not tied to specific transactions or a specific percentage of transactions closing, or a profit sharing plan that benefits all employees. A person solely responsible for credit administration or risk management is also not considered part of a creditor's loan production function. Credit administration and risk management includes, for example, loan underwriting, loan closing functions (e.g., loan documentation), disbursing funds, collecting mortgage payments and otherwise servicing the loan (e.g., escrow management and payment of taxes), monitoring loan performance, and foreclosure processing.*

Section 4: When Credit Extension is Prohibited
12 C.F.R. § 1026.42(e)

When Credit Extension is Prohibited - 12 CFR § 1026.42(e)

Regulatory Discussion

With respect to a consumer credit transaction that is secured by the consumer's principal dwelling, this section generally prohibits a creditor from extending credit based on a valuation that the creditor knows (at or before consummation) is in violation of either paragraph (c) or (d), above; unless the creditor documents it has acted with "reasonable diligence" to determine the valuation does not "materially misstate or misrepresent" the value of the dwelling.

Note the explanations of "materially misstate or misrepresent" in the regulatory text and "reasonable diligence" in the commentary.

Regulatory Text

(e) **When extension of credit prohibited.** In connection with a covered transaction, a creditor that knows, at or before consummation, of a violation of paragraph (c) or (d) of this section in connection with a valuation shall not extend credit based on the valuation, unless the creditor documents that it has acted with reasonable diligence to determine that the valuation does not materially misstate or misrepresent the value of the consumer's principal dwelling. For purposes of this paragraph (e), a valuation materially misstates or misrepresents the value of the consumer's principal dwelling if the valuation contains a misstatement or misrepresentation that affects the credit decision or the terms on which credit is extended.

Regulatory Commentary

42(e) When Extension of Credit Prohibited

*1. **Reasonable diligence.** A creditor will be deemed to have acted with reasonable diligence under §1026.42(e) if the creditor extends credit based on a valuation other than the valuation subject to the restriction in §1026.42(e). A creditor need not obtain a second valuation to document that the creditor has acted with reasonable diligence to determine that the valuation does not materially misstate or misrepresent the value of the consumer's principal dwelling, however. For example, assume an appraiser notifies a creditor before consummation that a loan originator attempted to cause the value assigned to the consumer's principal dwelling to be based on a factor other than the appraiser's independent judgment, through coercion. If the creditor reasonably determines and documents that the appraisal does not materially misstate or misrepresent the value of the consumer's principal dwelling, for purposes of §1026.42(e), the creditor may extend credit based on the appraisal.*

Section 5: Customary & Reasonable Compensation 12 C.F.R. § 1026.42(f)

Requirement for Customary & Reasonable Compensation - 12 CFR § 1026.42(f)(1)

Regulatory Discussion

With respect to a consumer credit transaction that is secured by the consumer's principal dwelling, this section *permits the creditor* (and its agents) *to compensate a fee appraiser* for performing appraisal services that is "*customary and reasonable*" for comparable services in the "*geographic market*."

See the commentary for explanation of the italicized terms "*customary and reasonable*" and "*geographic market*."

Regulatory Text

(f) **Customary and reasonable compensation**

(1) **Requirement to provide customary and reasonable compensation to fee appraisers**. In any covered transaction, the creditor and its agents shall compensate a fee appraiser for performing appraisal services at a rate that is customary and reasonable for comparable appraisal services performed in the geographic market of the property being appraised. For purposes of paragraph (f) of this section, "agents" of the creditor do not include any fee appraiser as defined in paragraph (f)(4)(i) of this section.

Regulatory Commentary

42(f)(1) Requirement to Provide Customary and Reasonable Compensation to Fee Appraisers

1. ***Agents of the creditor.*** *Whether a person is an agent of the creditor is determined by applicable law; however, a "fee appraiser" as defined in paragraph (f)(4)(i) is not an agent of the creditor for purposes of paragraph (f), and therefore is not required to pay other fee appraisers customary and reasonable compensation under paragraph (f).*

2. ***Geographic market.*** *For purposes of paragraph (f), the "geographic market of the property being appraised" means the geographic market relevant to compensation levels for appraisal services. Depending on the facts and circumstances, the relevant geographic market may be a state, metropolitan statistical area (MSA), metropolitan division, area*

outside of an MSA, county, or other geographic area. For example, assume that fee appraisers who normally work only in County A generally accept $400 to appraise an attached single-family property in County A. Assume also that very few or no fee appraisers who work only in contiguous County B will accept a rate comparable to $400 to appraise an attached single-family property in County A. The relevant geographic market for an attached single-family property in County A may reasonably be defined as County A. On the other hand, assume that fee appraisers who normally work only in County A generally accept $400 to appraise an attached single-family property in County A. Assume also that many fee appraisers who normally work only in contiguous County B will accept a rate comparable to $400 to appraise an attached single-family property in County A. The relevant geographic market for an attached single-family property in County A may reasonably be defined to include both County A and County B.

3. ***Failure to perform contractual obligations.*** *Paragraph (f)(1) does not prohibit a creditor or its agent from withholding compensation from a fee appraiser for failing to meet contractual obligations, such as failing to provide the appraisal report or violating state or Federal appraisal laws in performing the appraisal.*

4. ***Agreement that fee is "customary and reasonable."*** *A document signed by a fee appraiser indicating that the appraiser agrees that the fee paid to the appraiser is "customary and reasonable" does not by itself create a presumption of compliance with §1026.42(f) or otherwise satisfy the requirement to pay a fee appraiser at a customary and reasonable rate.*

5. ***Volume-based discounts.*** *Section 1026.42(f)(1) does not prohibit a fee appraiser and a creditor (or its agent) from agreeing to compensation based on transaction volume, so long as the compensation is customary and reasonable. For example, assume that a fee appraiser typically receives $300 for appraisals from creditors with whom it does business; the fee appraiser, however, agrees to reduce the fee to $280 for a particular creditor, in exchange for a minimum number of assignments from the creditor.*

Presumption of Compliance - 12 CFR § 1026.42(f)(2)

Regulatory Discussion

This section states a creditor (and its agents) shall be *presumed to be in compliance* with paragraph (f)(1), above, if *both of two* conditions are met.

Regulatory Text

(2) **Presumption of compliance.** A creditor and its agents shall be presumed to comply with paragraph (f)(1) of this section if:

(i) The creditor or its agents compensate the fee appraiser in an amount that is reasonably related to recent rates paid for comparable appraisal services performed in the geographic market of the property being appraised. In determining this amount, a creditor or its agents shall review the factors below and make any adjustments to recent rates paid in the relevant geographic market necessary to ensure that the amount of compensation is reasonable:

(A) The type of property,

(B) The scope of work,

(C) The time in which the appraisal services are required to be performed,

(D) Fee appraiser qualifications,

(E) Fee appraiser experience and professional record, and

(F) Fee appraiser work quality; and

(ii) The creditor and its agents do not engage in any anticompetitive acts in violation of state or Federal law that affect the compensation paid to fee appraisers, including:

(A) Entering into any contracts or engaging in any conspiracies to restrain trade through methods such as price fixing or market allocation, as prohibited under section 1 of the Sherman Antitrust Act, 15 U.S.C. 1, or any other relevant antitrust laws; or

(B) Engaging in any acts of monopolization such as restricting any person from entering the relevant geographic market or causing any person to leave the relevant geographic market, as prohibited under section 2 of the Sherman Antitrust Act, 15 U.S.C. 2, or any other relevant antitrust laws.

Regulatory Commentary

42(f)(2) Presumption of Compliance

*1. **In general.** A creditor and its agent are presumed to comply with paragraph (f)(1) if the creditor or its agent meets the conditions specified in paragraph (f)(2) in determining the compensation paid to a fee appraiser. These conditions are not requirements for compliance but, if met, create a presumption that the creditor or its agent has complied with §1026.42(f)(1). A person may rebut this presumption with evidence that the amount of compensation paid to a fee appraiser was not customary and reasonable for reasons unrelated to the conditions in paragraph (f)(2)(i) or (f)(2)(ii). If a creditor or its agent does not meet one of the non-required conditions set forth in paragraph (f)(2), the creditor's and its agent's compliance with paragraph (f)(1) is determined based on all of the facts and circumstances without a presumption of either compliance or violation.*

Paragraph 42(f)(2)(i)

*1. **Two-step process for determining customary and reasonable rates.** Paragraph (f)(2)(i) sets forth a two-step process for a creditor or its agent to determine the amount of* *compensation that is customary and reasonable in a given transaction. First, the creditor or its agent must identify recent rates paid for comparable appraisal services in the relevant geographic market. Second, once recent rates have been identified, the creditor or its agent must review the factors listed in paragraph (f)(2)(i)(A)-(F) and make any appropriate adjustments to the rates to ensure that the amount of compensation is reasonable.*

2. ***Identifying recent rates.*** *Whether rates may reasonably be considered "recent" depends on the facts and circumstances. Generally, "recent" rates would include rates charged within one year of the creditor's or its agent's reliance on this information to qualify for the presumption of compliance under paragraph (f)(2). For purposes of the presumption of compliance under paragraph (f)(2), a creditor or its agent may gather information about recent rates by using a reasonable method that provides information about rates for appraisal services in the geographic market of the relevant property; a creditor or its agent may, but is not required to, use or perform a fee survey.*

3. ***Accounting for factors.*** *Once recent rates in the relevant geographic market have been identified, the creditor or its agent must review the factors listed in paragraph (f)(2)(i)(A)-(F) to determine the appropriate rate for the current transaction. For example, if the recent rates identified by the creditor or its agent were solely for appraisal assignments in which the scope of work required consideration of two comparable properties, but the current transaction required an appraisal that considered three comparable properties, the creditor or its agent might reasonably adjust the rate by an amount that accounts for the increased scope of work, in addition to making any other appropriate adjustments based on the remaining factors.*

Paragraph 42(f)(2)(i)(A)

1. ***Type of property.*** *The type of property may include, for example, detached or attached single-family property, condominium or cooperative unit, or manufactured home.*

Paragraph 42(f)(2)(i)(B)

1. *Scope of work. The scope of work may include, for example, the type of inspection (such as exterior only or both interior and exterior) or number of comparables required for the appraisal.*

Paragraph 42(f)(2)(i)(D)

1. ***Fee appraiser qualifications.*** *The fee appraiser qualifications may include, for example, a state license or certification in accordance with the minimum criteria issued by the Appraisal Qualifications Board of the Appraisal Foundation, or completion of continuing education courses on effective appraisal methods and related topics.*

2. ***Membership in professional appraisal organization.*** *Paragraph 42(f)(2)(i)(D) does not override state or Federal laws prohibiting the exclusion of an appraiser from consideration for an assignment solely by virtue of membership or lack of membership in any particular appraisal organization. See, e.g., 12 CFR 225.66(a).*

Paragraph 42(f)(2)(i)(E)

1. ***Fee appraiser experience and professional record.*** *The fee appraiser's level of experience may include, for example, the fee appraiser's years of service as a state-licensed or state-certified appraiser, or years of service appraising properties in a particular geographical area or of a particular type. The fee appraiser's professional record may include, for example, whether the fee appraiser has a past record of suspensions, disqualifications, debarments, or judgments for waste, fraud, abuse or breach of legal or professional standards.*

Paragraph 42(f)(2)(i)(F)

1. ***Fee appraiser work quality.*** *The fee appraiser's work quality may include, for example, the past quality of appraisals performed by the appraiser based on the written performance and review criteria of the creditor or agent of the creditor.*

Paragraph 42(f)(2)(ii)

1. ***Restraining trade.*** *Under §1026.42(f)(2)(ii)(A), creditor or its agent would not qualify for the presumption of compliance under paragraph (f)(2) if it engaged in any acts to restrain trade such as entering into a price fixing or market allocation agreement that affect the compensation of fee appraisers. For example, if appraisal management company A and appraisal management company B agreed to compensate fee appraisers at no more than a specific rate or range of rates, neither appraisal management company would qualify for the presumption of compliance. Likewise, if appraisal management company A and appraisal management company B agreed that appraisal management company A would limit its business to a certain portion of the relevant geographic market and appraisal management company B would limit its business to a different portion of the relevant geographic market, and as a result each appraisal management company unilaterally set the fees paid to fee appraisers in their respective portions of the market, neither appraisal management company would qualify for the presumption of compliance under paragraph (f)(2).*
2. ***Acts of monopolization.*** *Under §1026.42(f)(2)(ii)(B), a creditor or its agent would not qualify for the presumption of compliance under paragraph (f)(2) if it engaged in any act of monopolization such as restricting entry into the relevant geographic market or causing any person to leave the relevant geographic market, resulting in anticompetitive effects that affect the compensation paid to fee appraisers. For example, if only one appraisal management company exists or is predominant in a particular market area, that appraisal management company might not qualify for the presumption of compliance if it entered into exclusivity agreements with all creditors in the market or all fee appraisers in the market, such that other appraisal management companies had to leave or could not enter the market. Whether this behavior would be considered an anticompetitive act that affects the compensation paid to fee appraisers depends on all of the facts and circumstances, including applicable law.*

Alternative Presumption of Compliance - 12 CFR § 1026.42(f)(3)

Regulatory Discussion

This section provides an *alternative presumption of compliance* with paragraph (f)(1), above, if the creditor (or its agents) determine the amount of compensation paid to the fee appraiser meets <u>*each of three*</u> conditions.

Regulatory Text

(3) **Alternative presumption of compliance.** A creditor and its agents shall be presumed to comply with paragraph (f)(1) of this section if the creditor or its agents determine the amount of compensation paid to the fee appraiser by relying on information about rates that:

(i) Is based on objective third-party information, including fee schedules, studies, and surveys prepared by independent third parties such as government agencies, academic institutions, and private research firms;

(ii) Is based on recent rates paid to a representative sample of providers of appraisal services in the geographic market of the property being appraised or the fee schedules of those providers; and

(iii) In the case of information based on fee schedules, studies, and surveys, such fee schedules, studies, or surveys, or the information derived therefrom, excludes compensation paid to fee appraisers for appraisals ordered by appraisal management companies, as defined in paragraph (f)(4)(iii) of this section.

Regulatory Commentary

42(f)(3) Alternative Presumption of Compliance

1. ***In general.*** *A creditor and its agent are presumed to comply with paragraph (f)(1) if the creditor or its agent determine the compensation paid to a fee appraiser based on information about customary and reasonable rates that satisfies the conditions in paragraph (f)(3) for that information. Reliance on information satisfying the conditions in paragraph (f)(3) is not a requirement for compliance with paragraph (f)(1), but creates a presumption that the creditor or its agent has complied. A person may rebut this presumption with evidence that the rate of compensation paid to a fee appraiser by the creditor or its agent is not customary and reasonable based on facts or information other than third-party information satisfying the conditions of this paragraph (f)(3). If a creditor or its agent does not rely on information that meets the conditions in paragraph (f)(3), the creditor's and its agent's compliance with paragraph (f)(1) is determined based on all of the facts and circumstances without a presumption of either compliance or violation.*

2. ***Geographic market.*** *The meaning of "geographic market" for purposes of paragraph (f) is explained in comment (f)(1)-1.*

*3. **Recent rates.** Whether rates may reasonably be considered "recent" depends on the facts and circumstances. Generally, "recent" rates would include rates charged within one year of the creditor's or its agent's reliance on this information to qualify for the presumption of compliance under paragraph (f)(3).*

Definitions - 12 CFR § 1026.42(f)(4)

Regulatory Discussion

This section provides definitions of three terms specific to this paragraph (f).

Regulatory Text

(4) **Definitions.** For purposes of this paragraph (f), the following definitions apply:

(i) **Fee appraiser.** The term "fee appraiser" means:

(A) A natural person who is a state-licensed or state-certified appraiser and receives a fee for performing an appraisal, but who is not an employee of the person engaging the appraiser; or

(B) An organization that, in the ordinary course of business, employs state-licensed or state-certified appraisers to perform appraisals, receives a fee for performing appraisals, and is not subject to the requirements of section 1124 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (12 U.S.C. 3353).

(ii) **Appraisal services.** The term "appraisal services" means the services required to perform an appraisal, including defining the scope of work, inspecting the property, reviewing necessary and appropriate public and private data sources (for example, multiple listing services, tax assessment records and public land records), developing and rendering an opinion of value, and preparing and submitting the appraisal report.

(iii) **Appraisal management company.** The term "appraisal management company" means any person authorized to perform one or more of the following actions on behalf of the creditor:

(A) Recruit, select, and retain fee appraisers;

(B) Contract with fee appraisers to perform appraisal services;

(C) Manage the process of having an appraisal performed, including providing administrative services such as receiving appraisal orders and appraisal reports, submitting completed appraisal reports to creditors and underwriters, collecting fees from creditors and underwriters for services provided, and compensating fee appraisers for services performed; or

(D) Review and verify the work of fee appraisers.

Regulatory Commentary

42(f)(4) Definitions

42(f)(4)(i) Fee Appraiser

1. ***Organization.*** *The term "organization" in paragraph 42(f)(4)(i)(B) includes a corporation, partnership, proprietorship, association, cooperative, or other business entity and does not include a natural person.*

Section 6: Mandatory Reporting
12 C.F.R. § 1026.42(g)

Mandatory Reporting - 12 CFR § 1026.42(g)

Regulatory Discussion

This section requires any creditor (or provider of settlement services) that reasonably believes an appraiser has not complied with the USPAP (or ethical or professional requirements) shall refer (within a reasonable period time) the matter to the appropriate state agency if the "*failure to comply is material*."

Note the explanation of the term "*failure to comply is material*" in the regulatory text and commentary.

Regulatory Text

(g) **Mandatory reporting**

(1) **Reporting required.** Any covered person that reasonably believes an appraiser has not complied with the Uniform Standards of Professional Appraisal Practice or ethical or professional requirements for appraisers under applicable state or Federal statutes or regulations shall refer the matter to the appropriate state agency if the failure to comply is material. For purposes of this paragraph (g)(1), a failure to comply is material if it is likely to significantly affect the value assigned to the consumer's principal dwelling.

(2) **Timing of reporting**. A covered person shall notify the appropriate state agency within a reasonable period of time after the person determines that there is a reasonable basis to believe that a failure to comply required to be reported under paragraph (g)(1) of this section has occurred.

(3) **Definition**. For purposes of this paragraph (g), "state agency" means "state appraiser certifying and licensing agency" under 12 U.S.C. 3350(1) and any implementing regulations. The appropriate state agency to which a covered person must refer a matter under paragraph (g)(1) of this section is the agency for the state in which the consumer's principal dwelling is located.

Regulatory Commentary

42(g) Mandatory Reporting

42(g)(1) Reporting Required

1. ***Reasonable basis.*** *A person reasonably believes that an appraiser has materially failed to comply with the Uniform Standards of Professional Appraisal Practice (USPAP) established by the Appraisal Standards Board of the Appraisal Foundation (as defined in 12 U.S.C. 3350(9)) or ethical or professional requirements for appraisers under applicable state or Federal statutes or regulations if the person possesses knowledge or information that would lead a reasonable person in the same circumstances to conclude that the appraiser has materially failed to comply with USPAP or such statutory or regulatory requirements.*

2. ***Material failure to comply.*** *For purposes of §1026.42(g)(1), a material failure to comply is one that is likely to affect the value assigned to the consumer's principal dwelling. The following are examples of a material failure to comply with USPAP or ethical or professional requirements:*

   i. Mischaracterizing the value of the consumer's principal dwelling in violation of §1026.42(c)(2)(i).

   ii. Performing an assignment in a grossly negligent manner, in violation of a rule under USPAP.

   iii. Accepting an appraisal assignment on the condition that the appraiser will report a value equal to or greater than the purchase price for the consumer's principal dwelling, in violation of a rule under USPAP.

3. ***Other matters.*** *Section 1026.42(g)(1) does not require reporting of a matter that is not material under §1026.42(g)(1), for example:*

   i. An appraiser's disclosure of confidential information in violation of applicable state law.

   ii. An appraiser's failure to maintain errors and omissions insurance in violation of applicable state law.

4. ***Examples of covered persons.*** *"Covered persons" include creditors, mortgage brokers, appraisers, appraisal management companies, real estate agents, and other persons that provide "settlement services" as defined in section 3(3) of the Real Estate Settlement Procedures Act (12 U.S.C. 2602(3)) and the implementing regulation at 12 CFR 1024.2. See §1026.42(b)(1).*

5. ***Examples of persons not covered.*** *The following persons are not "covered persons" (unless, of course, they are creditors with respect to a covered transaction or perform "settlement services" in connection with a covered transaction):*

   i. The consumer who obtains credit through a covered transaction.

   ii. A person secondarily liable for a covered transaction, such as a guarantor.

   iii. A person that resides in or will reside in the consumer's principal dwelling but will not be liable on the covered transaction, such as a non-obligor spouse.

6. ***Appraiser.*** *For purposes of §1026.42(g)(1), an "appraiser" is a natural person who provides opinions of the value of dwellings and is required to be licensed or certified under the laws of the state in which the consumer's principal dwelling is located or otherwise is subject to the jurisdiction of the appraiser certifying and licensing agency for that state. See 12 U.S.C. 3350(1).*

Section 7: Joint Rule
12 C.F.R. § 1026.42(h)

Joint Rule - 12 CFR § 1026.42(h)

Regulatory Discussion

This section refers to the CFPB's joint rule implementing FIRREA's appraisal management company minimum requirements as amended by the Dodd-Frank Act.

Regulatory Text

(h) The Bureau issued a joint rule to implement the appraisal management company minimum requirements in the Financial Institutions Reform, Recovery, and Enforcement Act, as amended by section 1473 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. *See* 12 CFR part 34.

Regulatory Commentary

None.

Ability to Repay (Mortgages)

Section 1: Repayment Ability [12 CFR § 1026.43(a)]

Introductory Commentary

Regulatory Discussion

For reference: §1026.25(c)(3) states a creditor shall retain evidence of compliance with §1026.43 of this regulation for three years after consummation of a transaction covered by that section.

Comments 25(c)(3)-1 and -2 state:

Evidence of compliance with repayment ability provisions. A creditor must retain evidence of compliance with §1026.43 for three years after the date of consummation of a consumer credit transaction covered by that section. (See comment 25(c)(3)-2 for guidance on the retention of evidence of compliance with the requirement to offer a consumer a loan without a prepayment penalty under §1026.43(g)(3).) If a creditor must verify and document information used in underwriting a transaction subject to §1026.43, the creditor shall retain evidence sufficient to demonstrate compliance with the documentation requirements of the rule. Although a creditor need not retain actual paper copies of the documentation used in underwriting a transaction subject to §1026.43, to comply with §1026.25(c)(3), the creditor must be able to reproduce such records accurately. For example, if the creditor uses a consumer's Internal Revenue Service (IRS) Form W-2 to verify the consumer's income, the creditor must be able to reproduce the IRS Form W-2 itself, and not merely the income information that was contained in the form.

Dwelling-secured transactions and prepayment penalties. If a transaction covered by §1026.43 has a prepayment penalty, the creditor must maintain records that document that the creditor complied with requirements for offering the consumer an alternative transaction that does not include a prepayment penalty under §1026.43(g)(3), (4), or (5). However, the creditor need not maintain records that document compliance with those provisions if a transaction is consummated without a prepayment penalty or if the creditor and consumer do not consummate a covered transaction. If a creditor offers a transaction with a prepayment penalty to a consumer through a mortgage broker, to evidence compliance with §1026.43(g)(4) the creditor should retain evidence of the alternative covered transaction presented to the mortgage broker, such as a rate sheet, and the agreement with the mortgage broker required by §1026.43(g)(4)(ii).

Regulatory Text

None.

Regulatory Commentary

Section 1026.43—Minimum Standards for Transactions Secured by a Dwelling

1. ***Record retention.*** *See §1026.25(c)(3) and comments 25(c)(3)-1 and -2 for guidance on the required retention of records as evidence of compliance with §1026.43.*

Scope – 12 CFR § 1026.43(a)

Regulatory Discussion

This section applies to any consumer credit transaction that is secured by a dwelling, including any real property attached to a dwelling. Excluded from these requirements are:

- HELOCs
- Timeshares
- Reverse mortgages
- Temporary or "bridge" loans
- Construction loans (no longer than 12 months
- Other loan types, that most banks do not offer

Regulatory Text

(a) **Scope.** This section applies to any consumer credit transaction that is secured by a dwelling, as defined in §1026.2(a)(19), including any real property attached to a dwelling, other than:

(1) A home equity line of credit subject to §1026.40;

(2) A mortgage transaction secured by a consumer's interest in a timeshare plan, as defined in 11 U.S.C. 101(53(D)); or

(3) For purposes of paragraphs (c) through (f) of this section:

(i) A reverse mortgage subject to §1026.33;

(ii) A temporary or "bridge" loan with a term of 12 months or less, such as a loan to finance the purchase of a new dwelling where the consumer plans to sell a current dwelling within 12 months or a loan to finance the initial construction of a dwelling;

(iii) A construction phase of 12 months or less of a construction-to-permanent loan;

(iv) An extension of credit made pursuant to a program administered by a Housing Finance Agency, as defined under 24 CFR 266.5;

(v) An extension of credit made by:

[Paragraphs A through D Omitted, as these provisions do not impact banks.]

(vi) An extension of credit made pursuant to a program authorized by sections 101 and 109 of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5211; 5219);

(vii) Consumer credit transactions that meet the following criteria…

[Paragraphs A through F Omitted, as these provisions do not impact banks.]

Regulatory Commentary

43(a) Scope.

1. ***Consumer credit.*** *In general, §1026.43 applies to consumer credit transactions secured by a dwelling, but certain dwelling-secured consumer credit transactions are exempt or partially exempt from coverage under §1026.43(a)(1) through (3). (See §1026.2(a)(12) for the definition of "consumer credit.") Section 1026.43 does not apply to an extension of credit primarily for a business, commercial, or agricultural purpose, even if it is secured by a dwelling. See §1026.3 and associated commentary for guidance in determining the primary purpose of an extension of credit. In addition, §1026.43 does not apply to any change to an existing loan that is not treated as a refinancing under §1026.20(a).*

2. ***Real property.*** *"Dwelling" means a residential structure that contains one to four units, whether or not the structure is attached to real property. See §1026.2(a)(19). For purposes of §1026.43, the term "dwelling" includes any real property to which the residential structure is attached that also secures the covered transaction. For example, for purposes of §1026.43(c)(2)(i), the value of the dwelling that secures the covered transaction includes the value of any real property to which the residential structure is attached that also secures the covered transaction.*

Paragraph 43(a)(3).

1. ***Renewable temporary or "bridge" loan.*** *Under §1026.43(a)(3)(ii), a temporary or "bridge" loan with a term of 12 months or less is exempt from §1026.43(c) through (f). Examples of such a loan are a loan to finance the purchase of a new dwelling where the consumer plans to sell a current dwelling within 12 months and a loan to finance the initial construction of a dwelling. Where a temporary or "bridge loan" is renewable, the loan term does not include any additional period of time that could result from a renewal provision provided that any renewal possible under the loan contract is for one year or less. For example, if a construction loan has an initial loan term of 12 months but is renewable for another 12-month loan term, the loan is exempt from §1026.43(c) through (f) because the initial loan term is 12 months.*

2. ***Construction phase of a construction-to-permanent loan.*** *Under §1026.43(a)(3)(iii), a construction phase of 12 months or less of a construction-to-permanent loan is exempt from §1026.43(c) through (f). A construction-to-permanent loan is a potentially multiple-advance loan to finance the construction, rehabilitation, or improvement of a dwelling that may be permanently financed by the same creditor. For such a loan, the construction phase and the permanent phase may be treated as separate transactions for the purpose of compliance with §1026.43(c) through (f), and the construction phase of the loan is exempt from §1026.43(c) through (f), provided the initial term is 12 months or less. See §1026.17(c)(6)(ii), allowing similar treatment for disclosures. Where the construction phase of a construction-to-permanent loan is renewable for a period of one year or less, the term of that construction phase does not include any additional period of time that could result from a renewal provision. For example, if the construction phase of a construction-to-permanent loan has an initial term of 12 months but is renewable for another 12-month term before permanent financing begins, the construction phase is exempt from §1026.43(c) through (f) because the initial term is 12 months. Any renewal of one year or less also qualifies for the exemption. The permanent phase of the loan is treated as a separate transaction and is not exempt under §1026.43(a)(3)(iii). It may be a qualified mortgage if it satisfies the appropriate requirements.*

Paragraph 43(a)(3)(iv) through (vii).

[Omitted, as these provisions do not impact banks.]

Section 2: Definitions
12 CFR § 1026.43(b)

Introduction

All definitions below are specific to this section of the regulation. We have elected to omit them from this manual, as they are mostly common sense and would add many additional pages.

Section 3: Repayment Ability
12 CFR § 1026.43(c)

General Requirement - 12 CFR § 1026.43(c)(1)

Regulatory Discussion

In general, a creditor cannot extend *credit to a consumer that is secured by a dwelling* (a "covered transaction") unless there is a *reasonable and good faith determination* that the consumer will have a *reasonable ability to repay* the loan.

There are numerous considerations discussed in the commentary.

Regulatory Text

(1) **General requirement.** A creditor shall not make a loan that is a covered transaction unless the creditor makes a reasonable and good faith determination at or before consummation that the consumer will have a reasonable ability to repay the loan according to its terms.

Regulatory Commentary

*1. **Reasonable and good faith determination.***

*i. **General.** Creditors generally are required by §1026.43(c)(1) to make reasonable and good faith determinations of consumers' ability to repay. Section 1026.43(c) and the accompanying commentary describe certain requirements for making this ability-to-repay determination, but do not provide comprehensive underwriting standards to which creditors must adhere. For example, the rule and commentary do not specify how much income is needed to support a particular level of debt or how credit history should be weighed against other factors. So long as creditors consider the factors set forth in §1026.43(c)(2) according to the requirements of §1026.43(c), creditors are permitted to develop their own underwriting standards and make changes to those standards over time in response to empirical information and changing economic and other conditions. Whether a particular ability-to-repay determination is reasonable and in good faith will depend not only on the underwriting standards adopted by the creditor, but on the facts and circumstances of an individual extension of credit and how a creditor's underwriting standards were applied to those facts and circumstances. A consumer's statement or attestation that the consumer has the ability to repay the loan is not indicative of whether the creditor's determination was reasonable and in good faith.*

*ii. **Considerations.***

A. The following may be evidence that a creditor's ability-to-repay determination was reasonable and in good faith:

1. The consumer demonstrated actual ability to repay the loan by making timely payments, without modification or accommodation, for a significant period of time *after consummation or, for an adjustable-rate, interest-only, or negative-amortization mortgage, for a significant period of time after recast;*

2. *The creditor used underwriting standards that have historically resulted in comparatively low rates of delinquency and default during adverse economic conditions; or*

3. *The creditor used underwriting standards based on empirically derived, demonstrably and statistically sound models.*

B. *In contrast, the following may be evidence that a creditor's ability-to-repay determination was not reasonable or in good faith:*

1. *The consumer defaulted on the loan a short time after consummation or, for an adjustable-rate, interest-only, or negative-amortization mortgage, a short time after recast;*

2. *The creditor used underwriting standards that have historically resulted in comparatively high levels of delinquency and default during adverse economic conditions;*

3. *The creditor applied underwriting standards inconsistently or used underwriting standards different from those used for similar loans without reasonable justification;*

4. *The creditor disregarded evidence that the underwriting standards it used are not effective at determining consumers' repayment ability;*

5. *The creditor disregarded evidence that the consumer may have insufficient residual income to cover other recurring obligations and expenses, taking into account the consumer's assets other than the property securing the loan, after paying his or her monthly payments for the covered transaction, any simultaneous loans, mortgage-related obligations, and any current debt obligations; or*

6. *The creditor disregarded evidence that the consumer would have the ability to repay only if the consumer subsequently refinanced the loan or sold the property securing the loan.*

C. *All of the considerations listed in paragraphs (A) and (B) above may be relevant to whether a creditor's ability-to-repay determination was reasonable and in good faith. However, these considerations are not requirements or prohibitions with which creditors must comply, nor are they elements of a claim that a consumer must prove to establish a violation of the ability-to-repay requirements. For example, creditors are not required to validate their underwriting criteria using mathematical models. These considerations also are not absolute in their application; instead they exist on a continuum and may apply to varying degrees. For example, the longer a consumer successfully makes timely payments after consummation or recast the less likely it is that the creditor's determination of ability to repay was unreasonable or not in good faith. Finally, each of these considerations must be viewed in the context of all facts and circumstances relevant to a particular extension of credit. For example, in some cases inconsistent application of underwriting standards may indicate that a creditor is manipulating those standards to approve a loan despite a consumer's inability to repay. The creditor's ability-to-repay* *determination therefore may be unreasonable or in bad faith. However, in other cases inconsistently applied underwriting standards may be the result of, for example, inadequate training and may nonetheless yield a reasonable and good faith ability-to-repay determination in a particular case. Similarly, although an early payment default on a mortgage will often be persuasive evidence that the creditor did not have a reasonable and good faith belief in the consumer's ability to repay (and such evidence may even be sufficient to establish a prima facie case of an ability-to-repay violation), a particular ability-to-repay determination may be reasonable and in good faith even though the consumer defaulted shortly after consummation if, for example, the consumer experienced a sudden and unexpected loss of income. In contrast, an ability-to-repay determination may be unreasonable or not in good faith even though the consumer made timely payments for a significant period of time if, for example, the consumer was able to make those payments only by foregoing necessities such as food and heat.*

2. ***Repayment ability at consummation.*** *Section 1026.43(c)(1) requires the creditor to determine, at or before the time the loan is consummated, that a consumer will have a reasonable ability to repay the loan. A change in the consumer's circumstances after consummation (for example, a significant reduction in income due to a job loss or a significant obligation arising from a major medical expense) that cannot be reasonably anticipated from the consumer's application or the records used to determine repayment ability is not relevant to determining a creditor's compliance with the rule. However, if the application or records considered at or before consummation indicate there will be a change in a consumer's repayment ability after consummation (for example, if a consumer's application states that the consumer plans to retire within 12 months without obtaining new employment or that the consumer will transition from full-time to part-time employment), the creditor must consider that information under the rule.*

3. ***Interaction with Regulation B.*** *Section 1026.43(c)(1) does not require or permit the creditor to make inquiries or verifications prohibited by Regulation B, 12 CFR part 1002.*

Basis for Determination - 12 CFR § 1026.43(c)(2)

Regulatory Discussion

- The repayment ability determination requires consideration of the following eight items:
  - Income or assets
  - Employment status
  - Monthly payment on the proposed loan
  - Monthly payment on any simultaneous loan
  - Monthly payment for mortgage-related obligations
  - Other debts and obligations (i.e., alimony and child support)
  - monthly debt-to-income ratio or residual income
  - Consumer's credit history

The commentary provides additional important information on each of the eight items.

Regulatory Text

(2) **Basis for determination.** Except as provided otherwise in paragraphs (d), (e), and (f) of this section, in making the repayment ability determination required under paragraph (c)(1) of this section, a creditor must consider the following:

(i) The consumer's current or reasonably expected income or assets, other than the value of the dwelling, including any real property attached to the dwelling, that secures the loan;

(ii) If the creditor relies on income from the consumer's employment in determining repayment ability, the consumer's current employment status;

(iii) The consumer's monthly payment on the covered transaction, calculated in accordance with paragraph (c)(5) of this section;

(iv) The consumer's monthly payment on any simultaneous loan that the creditor knows or has reason to know will be made, calculated in accordance with paragraph (c)(6) of this section;

(v) The consumer's monthly payment for mortgage-related obligations;

(vi) The consumer's current debt obligations, alimony, and child support;

(vii) The consumer's monthly debt-to-income ratio or residual income in accordance with paragraph (c)(7) of this section; and

(viii) The consumer's credit history.

Regulatory Commentary

[Omitted.]

Verification Using Third-Party Records - 12 CFR § 1026.43(c)(3)

Regulatory Discussion

A creditor *must verify* a consumer's repayment ability using reasonably reliable third-party records.

A creditor *must verify* a consumer's income or assets using the techniques discussed in (c)(4).

If a creditor relies on income from a consumer's employment in determining repayment ability, the creditor *may verify* a consumer's employment status orally if the creditor prepares a record of the information obtained orally.

If a creditor relies on a consumer's credit report to verify a consumer's current debt obligations and a consumer's application states a current debt obligation not shown in the consumer's credit report, the creditor *need not independently verify* such an obligation.

The commentary provides additional guidance on these verifications.

Regulatory Text

(3) **Verification using third-party records.** A creditor must verify the information that the creditor relies on in determining a consumer's repayment ability under §1026.43(c)(2) using reasonably reliable third-party records, except that:

(i) For purposes of paragraph (c)(2)(i) of this section, a creditor must verify a consumer's income or assets that the creditor relies on in accordance with §1026.43(c)(4);

(ii) For purposes of paragraph (c)(2)(ii) of this section, a creditor may verify a consumer's employment status orally if the creditor prepares a record of the information obtained orally; and

(iii) For purposes of paragraph (c)(2)(vi) of this section, if a creditor relies on a consumer's credit report to verify a consumer's current debt obligations and a consumer's application states a current debt obligation not shown in the consumer's credit report, the creditor need not independently verify such an obligation.

Regulatory Commentary

[Omitted.]

Verification of Income or Assets - 12 CFR § 1026.43(c)(4)

Regulatory Discussion

A creditor *must verify* the amounts of income or assets that the creditor relies on to determine a consumer's ability to repay, using third-party records that provide reasonably reliable evidence of the consumer's income or assets.

A creditor *may verify* the consumer's income using a tax-return transcript issued by the Internal Revenue Service (IRS).

Other examples of items that may be used:

- Copies of tax returns
- IRS Form W-2s
- Payroll statements, including military Leave and Earnings Statements;
- Financial institution records (such as direct deposit information on statements
- Records from the consumer's employer

- Records from a Federal, State, or local government agency stating the consumer's income from benefits or entitlements;
- Receipts from the consumer's use of check cashing services
- Receipts from the consumer's use of a funds transfer service.

Regulatory Text

(4) **Verification of income or assets.** A creditor must verify the amounts of income or assets that the creditor relies on under §1026.43(c)(2)(i) to determine a consumer's ability to repay a covered transaction using third-party records that provide reasonably reliable evidence of the consumer's income or assets. A creditor may verify the consumer's income using a tax-return transcript issued by the Internal Revenue Service (IRS). Examples of other records the creditor may use to verify the consumer's income or assets include:

(i) Copies of tax returns the consumer filed with the IRS or a State taxing authority;

(ii) IRS Form W-2s or similar IRS forms used for reporting wages or tax withholding;

(iii) Payroll statements, including military Leave and Earnings Statements;

(iv) Financial institution records;

(v) Records from the consumer's employer or a third party that obtained information from the employer;

(vi) Records from a Federal, State, or local government agency stating the consumer's income from benefits or entitlements;

(vii) Receipts from the consumer's use of check cashing services; and

(viii) Receipts from the consumer's use of a funds transfer service.

Regulatory Commentary

43(c)(4) Verification of Income or Assets.

1. ***Income or assets relied on.*** *A creditor need consider, and therefore need verify, only the income or assets the creditor relies on to evaluate the consumer's repayment ability. See comment 43(c)(2)(i)-2. For example, if a consumer's application states that the consumer earns a salary and is paid an annual bonus and the creditor relies on only the consumer's salary to evaluate the consumer's repayment ability, the creditor need verify only the salary. See also comments 43(c)(3)-1 and -2.*

2. ***Multiple applicants.*** *If multiple consumers jointly apply for a loan and each lists income or assets on the application, the creditor need verify only the income or assets the creditor relies on in determining repayment ability. See comment 43(c)(2)(i)-5.*

3. ***Tax-return transcript.*** *Under §1026.43(c)(4), a creditor may verify a consumer's income using an Internal Revenue Service (IRS) tax-return transcript, which summarizes the information in* *a consumer's filed tax return, another record that provides reasonably reliable evidence of the consumer's income, or both. A creditor may obtain a copy of a tax-return transcript or a filed tax return directly from the consumer or from a service provider. A creditor need not obtain the copy directly from the IRS or other taxing authority. See comment 43(c)(3)-2.*

Paragraph 43(c)(4)(vi).

*1. **Government benefits.** In verifying a consumer's income, a creditor may use a written or electronic record from a government agency of the amount of any benefit payments or awards, such as a "proof of income letter" issued by the Social Security Administration (also known as a "budget letter," "benefits letter," or "proof of award letter").*

Payment Calculation - 12 CFR § 1026.43(c)(5)

Regulatory Discussion

In general, whether the loan is a fixed-rate, adjustable-rate or step-rate mortgage, the consumer's *monthly payment calculation must be made* using:

- the fully indexed rate or any introductory interest rate, whichever is greater; and
- monthly, fully amortizing payments that are substantially equal.

There are *special rules for*:

- Loans with a balloon payment, the monthly payment calculation *must be made* using:
- The maximum payment scheduled during the first five years for non-HPML
- The maximum payment in the payment schedule, including the balloon payment, for an HPML
- Interest-only loans, the monthly payment calculation *must be made* using:
- The fully indexed rate or any introductory interest rate, whichever is greater
- 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 switches to payments.

Negative amortization loans, the monthly payment calculation *must be made* using:

- The fully indexed rate or any introductory interest rate, whichever is greater
- Substantially equal, monthly payments of principal and interest that will repay the maximum loan amount over the term of the loan remaining as of the date the loan reaches the maximum loan amount.

The commentary provides additional important information on these rules.

Regulatory Text

(5) **Payment calculation**

(i) **General rule.** Except as provided in paragraph (c)(5)(ii) of this section, a creditor must make the consideration required under paragraph (c)(2)(iii) of this section using:

(A) The fully indexed rate or any introductory interest rate, whichever is greater; and

(B) Monthly, fully amortizing payments that are substantially equal.

(ii) **Special rules for loans with a balloon payment, interest-only loans, and negative amortization loans.** A creditor must make the consideration required under paragraph (c)(2)(iii) of this section for:

(A) A loan with a balloon payment, as defined in §1026.18(s)(5)(i), using:

(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 covered transaction; or

(2) The maximum payment in the payment schedule, including any balloon payment, for a higher-priced covered transaction;

(B) An interest-only loan, as defined in §1026.18(s)(7)(iv), using:

(1) The fully indexed rate or any introductory interest rate, whichever is greater; 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.

(C) A negative amortization loan, as defined in §1026.18(s)(7)(v), using:

(1) The fully indexed rate or any introductory interest rate, whichever is greater; and

(2) Substantially equal, monthly payments of principal and interest that will repay the maximum loan amount over the term of the loan remaining as of the date the loan is recast.

Regulatory Commentary

[Omitted.]

Payment Calculation Simultaneous Loans - 12 CFR § 1026.43(c)(6)

Regulatory Discussion

When calculating a consumer's monthly payment in accordance with paragraph (c)(5), a creditor must consider the consumer's payment on any simultaneous loan either:

- For a "covered transaction" (any consumer credit transaction that is secured by a dwelling), by following the rules in paragraph (c)(5); or
- For a HELOC, by using the payment required by the HELOC and the amount of the "covered transaction."

Regulatory Text

(6) **Payment calculation for simultaneous loans.** For purposes of making the evaluation required under paragraph (c)(2)(iv) of this section, a creditor must consider, taking into account any mortgage-related obligations, a consumer's payment on a simultaneous loan that is:

(i) A covered transaction, by following paragraph (c)(5)of this section; or

(ii) A home equity line of credit subject to §1026.40, by using the periodic payment required under the terms of the plan and the amount of credit to be drawn at or before consummation of the covered transaction.

Regulatory Commentary

43(c)(6) Payment calculation for simultaneous loans.

1. ***Scope.*** *In determining the consumer's repayment ability for a covered transaction under §1026.43(c)(2)(iii), a creditor must include consideration of any simultaneous loan which it knows, or has reason to know, will be made at or before consummation of the covered transaction. For a discussion of the standard "knows or has reason to know," see comment 43(c)(2)(iv)-2. For the meaning of the term "simultaneous loan," see §1026.43(b)(12).*

2. ***Payment calculation—covered transaction.*** *For a simultaneous loan that is a covered transaction, as that term is defined under §1026.43(b)(1), a creditor must determine a consumer's ability to repay the monthly payment obligation for a simultaneous loan as set forth in §1026.43(c)(5), taking into account any mortgage-related obligations required to be considered under §1026.43(c)(2)(v). For the meaning of the term "mortgage-related obligations," see §1026.43(b)(8).*

3. ***Payment calculation—home equity line of credit.*** *For a simultaneous loan that is a home equity line of credit subject to §1026.40, the creditor must consider the periodic payment required under the terms of the plan when assessing the consumer's ability to repay the covered transaction secured by the same dwelling as the simultaneous loan. Under §1026.43(c)(6)(ii), a creditor must determine the periodic payment required under the terms of the plan by considering the actual amount of credit to be drawn by the consumer at consummation of the covered transaction. The amount to be drawn is the amount requested by the consumer; when the amount requested will be disbursed, or actual receipt of funds, is not determinative. Any additional draw against the line of credit that the creditor of the covered transaction does not know or have reason to know about before or during underwriting need not be considered in relation to ability to repay. For example, where the creditor's policies and procedures require the source of down payment to be verified, and the creditor verifies that a simultaneous loan that is a HELOC will provide the source of down payment for the first-lien covered transaction,* *the creditor must consider the periodic payment on the HELOC by assuming the amount drawn is at least the down payment amount. In general, a creditor should determine the periodic payment based on guidance in the commentary to §1026.40(d)(5) (discussing payment terms).*

Monthly DTI Ratio or Residual Income - 12 CFR § 1026.43(c)(7)

Regulatory Discussion

If a creditor considers the consumer's monthly 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."

If a creditor considers the consumer's monthly residual income the creditor must consider the consumer's remaining income after subtracting the consumer's "total monthly debt obligations" from the "total monthly income."

Definitions are provided for:

- Total monthly debt obligations.
- Total monthly income

The commentary provides additional considerations.

Regulatory Text

(7) **Monthly debt-to-income ratio or residual income**

(i) **Definitions.** For purposes of this paragraph (c)(7), the following definitions apply:

(A) **Total monthly debt obligations.** The term *total monthly debt obligations* means the sum of: the payment on the covered transaction, as required to be calculated by paragraphs (c)(2)(iii) and (c)(5) of this section; simultaneous loans, as required by paragraphs (c)(2)(iv) and (c)(6) of this section; mortgage-related obligations, as required by paragraph (c)(2)(v) of this section; and current debt obligations, alimony, and child support, as required by paragraph (c)(2)(vi) of this section.

(B) **Total monthly income.** The term *total monthly income* means the sum of the consumer's current or reasonably expected income, including any income from assets, as required by paragraphs (c)(2)(i) and (c)(4) of this section.

(ii) **Calculations**

(A) **Monthly debt-to-income ratio.** If a creditor considers the consumer's monthly debt-to-income ratio under paragraph (c)(2)(vii) of this section, the creditor must consider the ratio of the consumer's total monthly debt obligations to the consumer's total monthly income.

(B) **Monthly residual income.** If a creditor considers the consumer's monthly residual income under paragraph (c)(2)(vii) of this section, the creditor must consider the consumer's remaining income after subtracting the consumer's total monthly debt obligations from the consumer's total monthly income.

Regulatory Commentary

43(c)(7) Monthly debt-to-income ratio or residual income.

*1. **Monthly debt-to-income ratio or monthly residual income.** Under §1026.43(c)(2)(vii), the creditor must consider the consumer's monthly debt-to-income ratio, or the consumer's monthly residual income, in accordance with the requirements in §1026.43(c)(7). In contrast to the qualified mortgage provisions in §1026.43(e), §1026.43(c) does not prescribe a specific monthly debt-to-income ratio with which creditors must comply. Instead, an appropriate threshold for a consumer's monthly debt-to-income ratio or monthly residual income is for the creditor to determine in making a reasonable and good faith determination of a consumer's ability to repay.*

*2. **Use of both monthly debt-to-income ratio and monthly residual income.** If a creditor considers the consumer's monthly debt-to-income ratio, the creditor may also consider the consumer's residual income as further validation of the assessment made using the consumer's monthly debt-to-income ratio.*

*3. **Compensating factors.** The creditor may consider factors in addition to the monthly debt-to-income ratio or residual income in assessing a consumer's repayment ability. For example, the creditor may reasonably and in good faith determine that a consumer has the ability to repay despite a higher debt-to-income ratio or lower residual income in light of the consumer's assets other than the dwelling, including any real property attached to the dwelling, securing the covered transaction, such as a savings account. The creditor may also reasonably and in good faith determine that a consumer has the ability to repay despite a higher debt-to-income ratio in light of the consumer's residual income.*

Section 4: Refinancing of Non-Standard Mortgages 12 CFR § 1026.43(d)

Definitions - 12 CFR § 1026.43(d)(1)

Regulatory Discussion

This section begins with the definition of three terms specific to this section.

Non-standard mortgage includes any consumer credit transaction that is secured by a dwelling that is:

- An ARM with an introductory fixed interest rate for a period of one year or longer;
- An interest-only loan
- A negative amortization loan

Standard mortgage includes any consumer credit transaction that is secured by a dwelling:

- That provides for regular periodic payments (*with conditions*)
- For which the total points and fees payable in connection with the transaction do not exceed specified amounts
- For which the term does not exceed 40 years
- For which the interest rate is fixed for at least the first five years after consummation
- For which the proceeds from the loan are used solely for specific purposes

Refinancing is defined in §1026.20(a)

The regulatory text and commentary has been omitted here.

Section 5: Qualified Mortgages
12 CFR § 1026.43(e)

Safe Harbor and Presumption of Compliance - 12 CFR § 1026.43(e)(1)

Regulatory Discussion

A safe harbor with the repayment ability requirements of paragraph (c) (discussed in Section 3, above) is provided to a creditor (or assignee) of:

- a "*qualified mortgage*" that
- <u>is not</u> a "*higher-priced covered transaction*"

A presumption of compliance with the repayment ability requirements of paragraph (c) (discussed in Section 3, above) is provided to a creditor (or assignee) of:

- a "*qualified mortgage*" that
- <u>is</u> a "*higher-priced covered transaction*"

To rebut the presumption of compliance, it must be proven:

- the creditor did not make a reasonable and good faith determination of the consumer's repayment ability,
- by showing that the consumer's income, debt obligations, alimony, child support, and the consumer's monthly payment
- would leave the consumer with insufficient residual income or assets with which to meet living expenses.

Regulatory Text

(1) **Safe harbor and presumption of compliance**

(i) **Safe harbor for loans that are not higher-priced covered transactions.** A creditor or assignee of a qualified mortgage, as defined in paragraphs (e)(2), (e)(4), (e)(5), (e)(6), or (f) of this section, that is not a higher-priced covered transaction, as defined in paragraph (b)(4) of this section, complies with the repayment ability requirements of paragraph (c) of this section.

(ii) **Presumption of compliance for higher-priced covered transactions.**

(A) A creditor or assignee of a qualified mortgage, as defined in paragraph (e)(2), (e)(4), (e)(5), (e)(6), or (f) of this section, that is a higher-priced covered transaction, as defined in paragraph (b)(4) of this section, is presumed to comply with the repayment ability requirements of paragraph (c) of this section.

(B) To rebut the presumption of compliance described in paragraph (e)(1)(ii)(A) of this section, it must be proven that, despite meeting the prerequisites of paragraph (e)(2), (e)(4), (e)(5), (e)(6), or (f) of this section, the creditor did not make a reasonable and good faith determination of the consumer's repayment ability at the time of consummation, by showing that the consumer's income, debt obligations, alimony, child support, and the consumer's monthly payment (including mortgage-related obligations) on the covered transaction and on any simultaneous loans of which the creditor was aware at consummation would leave the consumer with insufficient residual income or assets other than the value of the dwelling (including any real property attached to the dwelling) that secures the loan with which to meet living expenses, including any recurring and material non-debt obligations of which the creditor was aware at the time of consummation.

Regulatory Commentary

[Omitted.]

Qualified Mortgage Definition - 12 CFR § 1026.43(e)(2)

Regulatory Discussion

In general, "*qualified mortgage*" means a consumer credit transaction that is secured by a dwelling that satisfies the following six conditions:

- That provides for regular periodic payments that are substantially equal (*see additional limitations in (2)(i)(A) through (C)*)
- For which the loan term does not exceed 30 years
- For which the total points and fees payable in connection with the loan do not exceed specified amounts
- For which the creditor underwrites the loan, taking into account the monthly payment for mortgage-related obligations (*see requirements in (2)(iv)(A) and (B)(1) through (2)*)
- For which the creditor considers and verifies, at or before consummation, certain information (*see requirements in (2)(v)(A) and (B)*)
- For which the ratio of the consumer's total monthly debt to total monthly income at the time of consummation does not exceed 43 percent (*see calculation in (2)(vi)(A) and (B)(1) through (2)*)

Note: exceptions to this general definition will be covered in paragraphs (e)(4), (5) and (6) of this Section 5, as well as in paragraph (f) in Section 6.

The commentary provides additional substantial guidance on conditions (i), (ii), (iv), (v) and (vi).

Regulatory Text

(2) **Qualified mortgage defined—general**. Except as provided in paragraph (e)(4), (e)(5), (e)(6), or (f) of this section, a qualified mortgage is a covered transaction:

(i) That provides for regular periodic payments that are substantially equal, except for the effect that any interest rate change after consummation has on the payment in the case of an adjustable-rate or step-rate mortgage, that do not:

(A) Result in an increase of the principal balance;

(B) Allow the consumer to defer repayment of principal, except as provided in paragraph (f) of this section; or

(C) Result in a balloon payment, as defined in §1026.18(s)(5)(i), except as provided in paragraph (f) of this section;

(ii) For which the loan term does not exceed 30 years;

(iii) For which the total points and fees payable in connection with the loan do not exceed the amounts specified in paragraph (e)(3) of this section;

(iv) For which the creditor underwrites the loan, taking into account the monthly payment for mortgage-related obligations, using:

(A) The maximum interest rate that may apply during the first five years after the date on which the first regular periodic payment will be due; and

(B) Periodic payments of principal and interest that will repay either:

(1) The outstanding principal balance over the remaining term of the loan as of the date the interest rate adjusts to the maximum interest rate set forth in paragraph (e)(2)(iv)(A) of this section, assuming the consumer will have made all required payments as due prior to that date; or

(2) The loan amount over the loan term;

(v) For which the creditor considers and verifies at or before consummation the following:

(A) The consumer's current or reasonably expected income or assets other than the value of the dwelling (including any real property attached to the dwelling) that secures the loan, in accordance with appendix Q and paragraphs (c)(2)(i) and (c)(4) of this section; and

(B) The consumer's current debt obligations, alimony, and child support in accordance with appendix Q and paragraphs (c)(2)(vi) and (c)(3) of this section; and

(vi) For which the ratio of the consumer's total monthly debt to total monthly income at the time of consummation does not exceed 43 percent. For purposes of this paragraph (e)(2)(vi), the ratio of the consumer's total monthly debt to total monthly income is determined:

(A) Except as provided in paragraph (e)(2)(vi)(B) of this section, in accordance with the standards in appendix Q;

(B) Using the consumer's monthly payment on:

(1) The covered transaction, including the monthly payment for mortgage-related obligations, in accordance with paragraph (e)(2)(iv) of this section; and

(2) Any simultaneous loan that the creditor knows or has reason to know will be made, in accordance with paragraphs (c)(2)(iv) and (c)(6) of this section.

Regulatory Commentary

[Omitted.]

Limits on Points and Fees for Qualified Mortgages - 12 CFR § 1026.43(e)(3)

Regulatory Discussion

A consumer credit transaction that is secured by a dwelling <u>is not</u> a "*qualified mortgage*" (as defined in (e)(2), above) *unless* the total "*points and fees*" (defined in §1026.32(b)(1)) <u>do not exceed</u> the limits established in (3)(i)(A) through (E) as detailed in the regulatory text.

Note: these limits are adjusted annually on January 1st.

There are special rules for transactions consummated on or before January 10, 2021.

If the creditor (or assignee) determines after consummation that the total points and fees exceed the limits in paragraph (e)(3)(i), the loan <u>*is not precluded*</u> from being a "*qualified mortgage,*" *provided the conditions* in (e)(iii)(A), (B)(1) through (3), and (C) *are satisfied*.

In the event the special rules are applicable, the creditor (or assignee) must pay to the consumer the amount (that is not less than the sum) specified in (e)(iv)(A) and (B).

The commentary provides additional guidance on this information.

Regulatory Text

(3) **Limits on points and fees for qualified mortgages.**

(i) Except as provided in paragraph (e)(3)(iii) of this section, a covered transaction is not a qualified mortgage unless the transaction's total points and fees, as defined in §1026.32(b)(1), do not exceed:

(A) For a loan amount greater than or equal to $100,000 (indexed for inflation): 3 percent of the total loan amount;

(B) For a loan amount greater than or equal to $60,000 (indexed for inflation) but less than $100,000 (indexed for inflation): $3,000 (indexed for inflation);

(C) For a loan amount greater than or equal to $20,000 (indexed for inflation) but less than $60,000 (indexed for inflation): 5 percent of the total loan amount;

(D) For a loan amount greater than or equal to $12,500 (indexed for inflation) but less than $20,000 (indexed for inflation): $1,000 (indexed for inflation);

(E) For a loan amount less than $12,500 (indexed for inflation): 8 percent of the total loan amount.

(ii) The dollar amounts, including the loan amounts, in paragraph (e)(3)(i) of this section shall be adjusted annually on January 1 by the annual percentage change in the Consumer Price Index for All Urban Consumers (CPI-U) that was reported on the preceding June 1. See the official commentary to this paragraph (e)(3)(ii) for the current dollar amounts.

(iii) For covered transactions consummated on or before January 10, 2021, if the creditor or assignee determines after consummation that the transaction's total points and fees exceed the applicable limit under paragraph (e)(3)(i) of this section, the loan is not precluded from being a qualified mortgage, provided:

(A) The loan otherwise meets the requirements of paragraphs (e)(2), (e)(4), (e)(5), (e)(6), or (f) of this section, as applicable;

(B) The creditor or assignee pays to the consumer the amount described in paragraph (e)(3)(iv) of this section within 210 days after consummation and prior to the occurrence of any of the following events:

(1) The institution of any action by the consumer in connection with the loan;

(2) The receipt by the creditor, assignee, or servicer of written notice from the consumer that the transaction's total points and fees exceed the applicable limit under paragraph (e)(3)(i) of this section; or

(3) The consumer becoming 60 days past due on the legal obligation; and

(C) The creditor or assignee, as applicable, maintains and follows policies and procedures for post-consummation review of points and fees and for making payments to consumers in accordance with paragraphs (e)(3)(iii)(B) and (e)(3)(iv) of this section.

(iv) For purposes of paragraph (e)(3)(iii) of this section, the creditor or assignee must pay to the consumer an amount that is not less than the sum of the following:

(A) The dollar amount by which the transaction's total points and fees exceeds the applicable limit under paragraph (e)(3)(i) of this section; and

(B) Interest on the dollar amount described in paragraph (e)(3)(iv)(A) of this section, calculated using the contract interest rate applicable during the period from consummation until the payment described in this paragraph (e)(3)(iv) is made to the consumer.

Regulatory Commentary

[Omitted.]

Qualified Mortgage Defined – Special Rules - 12 CFR § 1026.43(e)(4)

Regulatory Discussion

As an exception to the general definition of a "*qualified mortgage*" in paragraph (e)(2), above, this paragraph (e)(4) also includes as a "qualified mortgage" transactions that not only satisfy the requirements of paragraphs (e)(2)(i) through (iii) but also satisfies:

One or more of the following criteria, which requires a loan (except with regard to matters wholly unrelated to ability to repay):

- be eligible:
  - to be purchased or guaranteed by the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation; or
  - to be purchased or guaranteed by any limited-life regulatory entity succeeding the charters of either entity, above;
- be eligible to be insured by the U.S. Department of Housing and Urban Development;
- be eligible to be guaranteed by the U.S. Department of Veteran Affairs;
- be eligible to be guaranteed by the U.S. Department of Agriculture; or
- be eligible to be insured by the Rural Housing Service.

Note: each special rule described above shall expire on the effective date of a rule issued by each respective agency; and, unless otherwise expired as stated herein, these special rules are only available for covered transactions consummated on or before January 10, 2021.

See the commentary for additional information.

Regulatory Text

(4) **Qualified mortgage defined - special rules**

(i) **General.** Notwithstanding paragraph (e)(2) of this section, a qualified mortgage is a covered transaction that satisfies:

(A) The requirements of paragraphs (e)(2)(i) through (iii) of this section; and

(B) One or more of the criteria in paragraph (e)(4)(ii) of this section.

(ii) **Eligible loans.** A qualified mortgage under this paragraph (e)(4) must be one of the following at consummation:

(A) A loan that is eligible, except with regard to matters wholly unrelated to ability to repay:

(1) To be purchased or guaranteed by the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation operating under the conservatorship or receivership of the Federal Housing Finance Agency pursuant to section 1367(a) of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4617(a)); or

(2) To be purchased or guaranteed by any limited-life regulatory entity succeeding the charter of either the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation pursuant to section 1367(i) of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4617(i));

(B) A loan that is eligible to be insured, except with regard to matters wholly unrelated to ability to repay, by the U.S. Department of Housing and Urban Development under the National Housing Act (12 U.S.C. 1707 *et seq.*);

(C) A loan that is eligible to be guaranteed, except with regard to matters wholly unrelated to ability to repay, by the U.S. Department of Veterans Affairs;

(D) A loan that is eligible to be guaranteed, except with regard to matters wholly unrelated to ability to repay, by the U.S. Department of Agriculture pursuant to 42 U.S.C. 1472(h); or

(E) A loan that is eligible to be insured, except with regard to matters wholly unrelated to ability to repay, by the Rural Housing Service.

(iii) **Sunset of special rules.**

(A) Each respective special rule described in paragraph (e)(4)(ii)(B), (C), (D), or (E) of this section shall expire on the effective date of a rule issued by each respective agency pursuant to its authority under TILA section 129C(b)(3)(ii) to define a qualified mortgage.

(B) Unless otherwise expired under paragraph (e)(4)(iii)(A) of this section, the special rules in this paragraph (e)(4) are available only for covered transactions consummated on or before January 10, 2021.

Regulatory Commentary

[Omitted.]

QM – Small Creditor Portfolio Loans - 12 CFR § 1026.43(e)(5)

Regulatory Discussion

As an exception to the general definition of a "*qualified mortgage*" in paragraph (e)(2), above, this paragraph (e)(5) also includes as a "qualified mortgage" transactions that not only satisfy the requirements of paragraphs of (e)(2) (except for (e)(2)(vi)) but also satisfies the requirements of (e)(5)(i)(B) through (D), below.

Note: a "qualified mortgage" extended under this exception immediately loses its status as such if legal title to the qualified mortgage is sold, assigned, or otherwise transferred to another person (see exceptions in (e)(5)(ii)(A) through (D), below.

See the commentary for additional information.

Regulatory Text

(5) **Qualified mortgage defined—small creditor portfolio loans.**

(i) Notwithstanding paragraph (e)(2) of this section, a qualified mortgage is a covered transaction:

(A) That satisfies the requirements of paragraph (e)(2) of this section other than the requirements of paragraph (e)(2)(vi) and without regard to the standards in appendix Q to this part;

(B) For which the creditor considers at or before consummation the consumer's monthly debt-to-income ratio or residual income and verifies the debt obligations and income used to determine that ratio in accordance with paragraph (c)(7) of this section, except that the calculation of the payment on the covered transaction for purposes of determining the consumer's total monthly debt obligations in paragraph (c)(7)(i)(A) shall be determined in accordance with paragraph (e)(2)(iv) of this section instead of paragraph (c)(5) of this section;

(C) That is not subject, at consummation, to a commitment to be acquired by another person, other than a person that satisfies the requirements of paragraph (e)(5)(i)(D) of this section; and

(D) For which the creditor satisfies the requirements stated in §1026.35(b)(2)(iii)(B) and (C).

(ii) A qualified mortgage extended pursuant to paragraph (e)(5)(i) of this section immediately loses its status as a qualified mortgage under paragraph (e)(5)(i) if legal title to the qualified mortgage is sold, assigned, or otherwise transferred to another person except when:

(A) The qualified mortgage is sold, assigned, or otherwise transferred to another person three years or more after consummation of the qualified mortgage;

(B) The qualified mortgage is sold, assigned, or otherwise transferred to a creditor that satisfies the requirements of paragraph (e)(5)(i)(D) of this section;

(C) The qualified mortgage is sold, assigned, or otherwise transferred to another person pursuant to a capital restoration plan or other action under 12 U.S.C. 1831o, actions or instructions of any person acting as conservator, receiver, or bankruptcy trustee, an order of a State or Federal government agency with jurisdiction to examine the creditor pursuant to State or Federal law, or an agreement between the creditor and such an agency; or

(D) The qualified mortgage is sold, assigned, or otherwise transferred pursuant to a merger of the creditor with another person or acquisition of the creditor by another person or of another person by the creditor.

Regulatory Commentary

[Omitted.]

QM Balloon Payment Loans - 12 CFR § 1026.43(e)(6)

Regulatory Discussion

Note: this exception only applies to transactions for which the application was received before April 1, 2016.

As an exception to the general definition of a "*qualified mortgage*" in paragraph (e)(2), above, this paragraph (e)(6) also includes as a "qualified mortgage" transactions that not only satisfy the requirements of paragraphs in (e)(2) but also:

- satisfies the requirements of paragraph (f) (in Section 6, below); and
- the creditor satisfies the requirements of §1026.35(b)(2)(iii)(B) and (C)

Regulatory Text

(6) **Qualified mortgage defined - temporary balloon-payment qualified mortgage rules.**

(i) Notwithstanding paragraph (e)(2) of this section, a qualified mortgage is a covered transaction:

(A) That satisfies the requirements of paragraph (f) of this section other than the requirements of paragraph (f)(1)(vi); and

(B) For which the creditor satisfies the requirements stated in §1026.35(b)(2)(iii)(B) and (C).

(ii) The provisions of this paragraph (e)(6) apply only to covered transactions for which the application was received before April 1, 2016.

Regulatory Commentary

None.

Section 6: Balloon Payment Qualified Mortgages 12 CFR § 1026.43(f)

Exemption – 12 CFR § 1026.43(f)(1)

Regulatory Discussion

As an exception to the general definition of a "*qualified mortgage*" in paragraph (e)(2), above, this paragraph (f)(1) also includes as a "qualified mortgage" transactions that not only satisfy the requirements of paragraphs in (e)(2) but also provides for a balloon payment, provided the six conditions in paragraphs (f)(1)(i) through (vi) are satisfied.

The commentary provides additional important information on each of the six conditions.

Regulatory Text

(1) ***Exemption.*** Notwithstanding paragraph (e)(2) of this section, a qualified mortgage may provide for a balloon payment, provided:

(i) The loan satisfies the requirements for a qualified mortgage in paragraphs (e)(2)(i)(A), (e)(2)(ii), (e)(2)(iii), and (e)(2)(v) of this section, but without regard to the standards in appendix Q;

(ii) The creditor determines at or before consummation that the consumer can make all of the scheduled payments under the terms of the legal obligation, as described in paragraph (f)(1)(iv) of this section, together with the consumer's monthly payments for all mortgage-related obligations and excluding the balloon payment, from the consumer's current or reasonably expected income or assets other than the dwelling that secures the loan;

(iii) The creditor considers at or before consummation the consumer's monthly debt-to-income ratio or residual income and verifies the debt obligations and income used to determine that ratio in accordance with paragraph (c)(7) of this section, except that the calculation of the payment on the covered transaction for purposes of determining the consumer's total monthly debt obligations in (c)(7)(i)(A) shall be determined in accordance with paragraph (f)(iv)(A) of this section, together with the consumer's monthly payments for all mortgage-related obligations and excluding the balloon payment;

(iv) The legal obligation provides for:

(A) Scheduled payments that are substantially equal, calculated using an amortization period that does not exceed 30 years;

(B) An interest rate that does not increase over the term of the loan; and

(C) A loan term of five years or longer.

(v) The loan is not subject, at consummation, to a commitment to be acquired by another person, other than a person that satisfies the requirements of paragraph (f)(1)(vi) of this section; and

(vi) The creditor satisfies the requirements stated in §1026.35(b)(2)(iii)(A), (B), and (C).

Regulatory Commentary

[Omitted.]

Transfer of Balloon Loans - 12 CFR § 1026.43(f)(2)

Regulatory Discussion

This paragraph provides that a balloon-payment "qualified mortgage" will immediately lose its status as such if legal title to the balloon-payment qualified mortgage is sold, assigned, or otherwise transferred to another person (subject to the exceptions in (f)(2)(i) through (iv).

The commentary provides additional information on each of the exceptions.

Regulatory Text

(2) **Post-consummation transfer of balloon-payment qualified mortgage.** A balloon-payment qualified mortgage, extended pursuant to paragraph (f)(1), immediately loses its status as a qualified mortgage under paragraph (f)(1) if legal title to the balloon-payment qualified mortgage is sold, assigned, or otherwise transferred to another person except when:

(i) The balloon-payment qualified mortgage is sold, assigned, or otherwise transferred to another person three years or more after consummation of the balloon-payment qualified mortgage;

(ii) The balloon-payment qualified mortgage is sold, assigned, or otherwise transferred to a creditor that satisfies the requirements of paragraph (f)(1)(vi) of this section;

(iii) The balloon-payment qualified mortgage is sold, assigned, or otherwise transferred to another person pursuant to a capital restoration plan or other action under 12 U.S.C. 1831o, actions or instructions of any person acting as conservator, receiver or bankruptcy trustee, an order of a State or Federal governmental agency with jurisdiction to examine the creditor pursuant to State or Federal law, or an agreement between the creditor and such an agency; or

(iv) The balloon-payment qualified mortgage is sold, assigned, or otherwise transferred pursuant to a merger of the creditor with another person or acquisition of the creditor by another person or of another person by the creditor.

Regulatory Commentary

[Omitted.]

Prepayment Penalties - 12 CFR § 1026.43(g)

Regulatory Discussion

In general, a consumer credit transaction that is secured by a dwelling *must not include* any *prepayment penalties* unless four conditions are satisfied.

1. The prepayment penalty is otherwise permitted by law;
2. The APR cannot increase after consummation;
3. The transaction meet the definition of a "qualified mortgage;" and
4. The transaction is not a "high-priced mortgage loan."

Regulatory Text

(g) **Prepayment penalties**

(1) **When permitted.** A covered transaction must not include a prepayment penalty unless:

(i) The prepayment penalty is otherwise permitted by law; and

(ii) The transaction:

(A) Has an annual percentage rate that cannot increase after consummation;

(B) Is a qualified mortgage under paragraph (e)(2), (e)(4), (e)(5), (e)(6), or (f) of this section; and

(C) Is not a higher-priced mortgage loan, as defined in §1026.35(a).

Regulatory Commentary

None.

Prepayment Penalty Limits - 12 CFR § 1026.43(g)(2)

Regulatory Discussion

If prepayment penalties are permitted, there are two limitations which must be applied; as detailed in (g)(2)(i) and (i)(A) and (B).

Regulatory Text

(2) **Limits on prepayment penalties.** A prepayment penalty:

(i) Must not apply after the three-year period following consummation; and

(ii) Must not exceed the following percentages of the amount of the outstanding loan balance prepaid:

(A) 2 percent, if incurred during the first two years following consummation; and

(B) 1 percent, if incurred during the third year following consummation.

Regulatory Commentary

43(g)(2) Limits on prepayment penalties.

*1. **Maximum period and amount.** Section 1026.43(g)(2) establishes the maximum period during which a prepayment penalty may be imposed and the maximum amount of the prepayment penalty. A covered transaction may include a prepayment penalty that may be imposed during a shorter period or in a lower amount than provided under §1026.43(g)(2). For example, a covered transaction may include a prepayment penalty that may be imposed for two years after consummation and that equals 1 percent of the amount prepaid in each of those two years.*

Alternative Offer Required - 12 CFR § 1026.43(g)(3)

Regulatory Discussion

If a creditor offers a consumer a credit transaction that is secured by a dwelling that contains a prepayment penalty, the creditor must also offer the consumer an alternative transaction without a prepayment penalty.

The alternative transaction, without a prepayment penalty, is subject to five conditions (as detailed in (g)(3)(i)(A) and (B), and (ii) through (v).

The commentary provides additional guidance on conditions (i), (iv) and (v).

Regulatory Text

(3) **Alternative offer required.** A creditor must not offer a consumer a covered transaction with a prepayment penalty unless the creditor also offers the consumer an alternative covered transaction without a prepayment penalty and the alternative covered transaction:

(i) Has an annual percentage rate that cannot increase after consummation and has the same type of interest rate as the covered transaction with a prepayment penalty; for purposes of this paragraph (g), the term "type of interest rate" refers to whether a transaction:

(A) Is a fixed-rate mortgage, as defined in §1026.18(s)(7)(iii); or

(B) Is a step-rate mortgage, as defined in §1026.18(s)(7)(ii);

(ii) Has the same loan term as the loan term for the covered transaction with a prepayment penalty;

(iii) Satisfies the periodic payment conditions under paragraph (e)(2)(i) of this section;

(iv) Satisfies the points and fees conditions under paragraph (e)(2)(iii) of this section, based on the information known to the creditor at the time the transaction is offered; and

(v) Is a transaction for which the creditor has a good faith belief that the consumer likely qualifies, based on the information known to the creditor at the time the creditor offers the covered transaction without a prepayment penalty.

Regulatory Commentary

[Omitted.]

Offer Through a Mortgage Broker - 12 CFR § 1026.43(g)(4)

Regulatory Discussion

If a creditor offers a consumer a credit transaction that is secured by a dwelling, *through a mortgage broker*, that contains a prepayment penalty, the creditor must also:

- present the mortgage broker an alternative transaction without a prepayment penalty that satisfies the five conditions of paragraph (g)(3), above; and
- establish an agreement with the broker that the consumer will be presented an alternative transaction without a prepayment penalty offered by either:
  - the creditor; or
  - another creditor.

The commentary provides additional information.

Regulatory Text

(4) **Offer through a mortgage broker.** If the creditor offers a covered transaction with a prepayment penalty to the consumer through a mortgage broker, as defined in §1026.36(a)(2), the creditor must:

(i) Present the mortgage broker an alternative covered transaction without a prepayment penalty that satisfies the requirements of paragraph (g)(3) of this section; and

(ii) Establish by agreement that the mortgage broker must present the consumer an alternative covered transaction without a prepayment penalty that satisfies the requirements of paragraph (g)(3) of this section, offered by:

(A) The creditor; or

(B) Another creditor, if the transaction offered by the other creditor has a lower interest rate or a lower total dollar amount of discount points and origination points or fees.

Regulatory Commentary

[Omitted.]

Creditor that is a Loan Originator - 12 CFR § 1026.43(g)(5)

Regulatory Discussion

If a creditor is a "loan originator" and presents a consumer a credit transaction that is secured by a dwelling *offered by a person to which the creditor would assign the transaction after consummation, the creditor must*:

- present the consumer an alternative transaction without a prepayment penalty that satisfies the five conditions of paragraph (g)(3), above, offered by:
  - the assignee; or
  - another person.

The commentary provides additional information.

Regulatory Text

(5) **Creditor that is a loan originator.** If the creditor is a loan originator, as defined in §1026.36(a)(1), and the creditor presents the consumer a covered transaction offered by a person to which the creditor would assign the covered transaction after consummation, the creditor must present the consumer an alternative covered transaction without a prepayment penalty that satisfies the requirements of paragraph (g)(3) of this section, offered by:

(i) The assignee; or

(ii) Another person, if the transaction offered by the other person has a lower interest rate or a lower total dollar amount of origination discount points and points or fees.

Regulatory Commentary

43(g)(5) Creditor that is a loan originator.

*1. **Loan originator.** The definition of "loan originator" in §1026.36(a)(1) applies for purposes of §1026.43(g)(5). Thus, a loan originator includes any creditor that satisfies the definition of loan originator but makes use of "table-funding" by a third party. See comment 36(a)-1.i and ii.*

*2. **Lower interest rate.** Under §1026.43(g)(5), a creditor that is a loan originator must present an alternative covered transaction without a prepayment penalty that satisfies the requirements of §1026.43(g)(3) offered by either the assignee for the covered transaction or another person, if that other person offers a transaction with a lower interest rate or a lower total dollar amount of origination points or fees or discount points. See comment 36(e)(3)-3 for guidance in determining which step-rate mortgage has a lower interest rate.*

Applicability - 12 CFR § 1026.43(g)(6)

Regulatory Discussion

This Section only applies if a consumer a credit transaction that is secured by a dwelling:

- is consummated with a prepayment penalty; and is not violated if:
- a transaction without a prepayment penalty is consummated; or
- a transaction is not consummated.

Regulatory Text

(6) **Applicability.** This paragraph (g) applies only if a covered transaction is consummated with a prepayment penalty and is not violated if:

(i) A covered transaction is consummated without a prepayment penalty; or

(ii) The creditor and consumer do not consummate a covered transaction.

Regulatory Commentary

None.

Section 8: Evasion; Open-End Credit
12 CFR § 1026.43(h)

Evasion; Open End Credit - 12 CFR § 1026.43(h)

Regulatory Discussion

This section simply prohibits a creditor from structuring a loan as an open-end plan (HELOC) to evade the requirements of §1026.43.

Regulatory Text

(h) **Evasion; open-end credit**. In connection with credit secured by a consumer's dwelling that does not meet the definition of open-end credit in §1026.2(a)(20), a creditor shall not structure the loan as an open-end plan to evade the requirements of this section.

Regulatory Commentary

43(h) Evasion; open-end credit.

*1. **Subject to closed-end credit rules.** Where a creditor documents a loan as open-end credit but the features and terms, or other circumstances, demonstrate that the loan does not meet the definition of open-end credit in §1026.2(a)(20), the loan is subject to the rules for closed-end credit, including §1026.43.*

Section 9: Appendix Q to Part 1026:
Standards for Determining Monthly Debt and Income

Introduction

The appendix is extensive, and has been omitted.