

REGULATORY ALERT

NATIONAL CREDIT UNION ADMINISTRATION
1775 DUKE STREET, ALEXANDRIA, VA 22314

DATE: July 2013 **NO:** 13-RA-05

TO: Federally Insured Credit Unions

SUBJ: New Escrow Requirements under the Truth in Lending Act

ENCL: [TILA Escrow Rule – Small Entity Compliance Guide](#)

Dear Board of Directors and Chief Executive Officers:

If your credit union originates a higher-priced mortgage loan (HPML)¹ secured by a first lien on a principal dwelling, you may have to collect escrow payments from your borrower for at least the first **five years**, regardless of the loan-to-value ratio.

Background

On January 10, 2013, the Consumer Financial Protection Bureau (CFPB) issued a final rule for escrow requirements under the Truth in Lending Act (TILA), amending Regulation Z and implementing provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).² On May 23, 2013, the CFPB issued clarifying and technical amendments to the final rule.³

Regulation Z continues to require creditors to establish an escrow account for an HPML secured by a first lien on a principal dwelling, to help ensure the borrower sets aside funds to pay property taxes, premiums for homeowners insurance, and other mortgage-related insurance required by the creditor. An escrow account must be established before consummation of the

¹ For purposes of the escrow requirements rule, a “higher-priced mortgage loan” is a closed-end consumer credit transaction secured by the borrower’s principal dwelling with an annual percentage rate (APR) that exceeds the average prime offer rate (APOR) for a comparable transaction, as of the date the interest rate is set: (1) by 1.5% or more for a first-lien conventional or conforming loan; or (2) by 2.5% or more for a first-lien jumbo loan. The Federal Financial Institutions Examination Council (FFIEC) publishes APOR tables on its website: <http://www.ffiec.gov/ratespread/aportables.htm>.

² Escrow Requirements under the Truth in Lending Act (Regulation Z). 12 CFR Part 1026. http://files.consumerfinance.gov/f/201301_cfpb_final-rule_escrow-requirements.pdf.

³ Amendments to the 2013 Escrows Final Rule under the Truth in Lending Act (Regulation Z). <https://www.federalregister.gov/articles/2013/05/23/2013-12125/amendments-to-the-2013-escrows-final-rule-under-the-truth-in-lending-act-regulation-z>.

loan. **The final rule lengthens the time for which a mandatory escrow account must be maintained, from one year to five years.**

The recent clarifying and technical amendments enable a creditor to determine whether a county is considered “rural” or “underserved” for application of the escrow requirements and other mortgage-related rules.⁴ The final TILA Escrow Rule became effective on June 1, 2013.

What Are the New Escrow Requirements?

Maintain escrow account for at least five years – The TILA Escrow Rule requires you to establish and maintain escrow accounts for first-lien HPMLs for at least five years, subject to the requirements of the rule and any applicable exceptions. You must maintain the escrow account until one of the following occurs:

- The underlying debt obligation is terminated; or
- After the five-year period, the borrower requests the escrow account be canceled.

If you cancel the escrow account at the member’s request, the unpaid principal balance of the loan must be less than 80 percent of the original value of the property securing the underlying debt obligation. Additionally, the borrower must not be currently delinquent or in default on the underlying obligation. **If the conditions above are *not* met, you will need to maintain the escrow account *beyond* five years.**

An escrow account for an HPML need not be established for:

- Transactions to finance the initial construction of a dwelling;
- Transactions secured by shares in a cooperative;⁵
- Temporary or “bridge” loans with terms of 12 months or less;
- Open-end credit (such as a home equity line of credit);
- Insurance premiums the borrower purchases but you do not require;
- Reverse mortgages; or
- Subordinate liens.

Which Credit Unions Are Exempt?

The final rule provides an exemption for mortgage loans extended by creditors that originate a limited number of first-lien, covered transactions, have assets below a certain threshold, operate predominantly in rural or underserved areas, and do not maintain escrow accounts on mortgage obligations they currently service.

⁴ Amendments to the 2013 Escrows Final Rule under the Truth in Lending Act (Regulation Z). <https://www.federalregister.gov/articles/2013/04/18/2013-09058/amendments-to-the-2013-escrows-final-rule-under-the-truth-in-lending-act-regulation-z>.

⁵ Cooperative (or co-op) housing complex, in which shares give the purchaser a propriety lease or occupancy agreement in the building owned by a corporation. Shares are allocated based on size and location of a living unit.

To be eligible for the exemption, a credit union must meet four conditions:

- Made 500 or fewer first lien mortgages, together with any affiliate,⁶ during the preceding calendar year;
- Had less than \$2 billion in total assets, as of December 31 of the preceding year;
- Originates more than half of its first lien mortgages in a rural or underserved area; and
- Does not escrow for any mortgage obligation currently serviced by the credit union or an affiliate.

However, if your credit union meets all four conditions and plans to *sell* HPML obligations to another entity that does *not* meet the exemption requirements, your credit union *will* have to establish an escrow account for any HPML covered by the rule.

Credit unions are permitted to offer an escrow account to accommodate distressed borrowers, and may continue to maintain escrow accounts established for HPML applications received before June 1, 2013.

Finally, you do not have to escrow insurance payments for homeowners in common interest communities where the governing body is required to purchase master insurance policies.

What Is A Rural Or Underserved Area?

For purposes of the TILA Escrow Rule, “rural” areas are defined using the Urban Influence Codes established by the U.S. Department of Agriculture’s Economic Research Service, and “underserved” areas are defined by reference to data collected under the Home Mortgage Disclosure Act (HMDA).

A creditor may rely, as a safe harbor, on the list of counties published by the CFPB to determine whether a county qualifies as rural or underserved for a particular calendar year.

On May 16, 2013, the CFPB published a final list of rural and underserved counties for use in implementing the escrow rule for first lien HPMLs.⁷ The list also impacts implementation of several other CFPB mortgage rules that take effect in January 2014, including the Ability-to-Repay/Qualified Mortgage Rule, the Home Ownership and Equity Protection Act (HOEPA) Rule, and the HPMLs Appraisal Rule.

What Guidance Is Available?

On April 18, 2013, the CFPB published a **Small Entity Compliance Guide** for the TILA Escrow Rule. A link to the guide is included near the top of this letter (see Enclosure).

⁶ For example, an affiliate of a federal credit union is a credit union service organization (CUSO), as provided in 12 CFR Part 712, that is controlled by the federal credit union. An affiliate of a federally insured state-chartered credit union is a company that is controlled by the credit union.

⁷ The final list is available at: <http://www.consumerfinance.gov/blog/final-list-of-rural-and-or-underserved-counties-for-use-in-2013/>.

The purpose of the CFPB guide is to provide a summary of the rule in plain language and “question and answer” format, highlighting issues that creditors and their business partners might find helpful to consider when implementing the rule. The guide should be especially useful to credit unions with limited legal and compliance staff.

If your credit union originates HPMLs secured by principal dwellings, you may find the CFPB guide helpful. The guide will help you determine whether the mortgage loans you originate are regulated by the TILA Escrow Rule, and if so, your compliance obligations.

The guide discusses exceptions that might apply to your credit union, including special rules for loans made by certain small creditors operating predominantly in rural or underserved markets, as well as special rules for loans secured by properties in common interest communities such as condominiums and planned unit developments.

While the guide provides an overview of the TILA Escrow Rule, it is not a substitute for the underlying regulation. Only the rule and its Official Interpretations can provide complete and definitive information regarding its requirements.

What Should You Do?

You should familiarize yourself with the TILA Escrow Rule and resources available. As outlined in the Small Entity Compliance Guide, your implementation plan should consider:

- Affected products, departments, and staff;
- Business-process, operational, and technology changes necessary for compliance;
- Critical impacts on key service providers or business partners;
- Training needs; and
- Other mortgage rules with overlapping compliance considerations.

You will find copies of the TILA Escrow Rule and other mortgage rules at:
<http://www.consumerfinance.gov/regulations>.

If you have questions, please contact NCUA’s Office of Consumer Protection (703-518-1140 or ComplianceMail@ncua.gov), your regional office, or state supervisory authority.

Sincerely,

/s/

Debbie Matz
Chairman