REGULATORY ALERT

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

DATE: **January 2014** **NO.:** **14-RA-02**

TO: **Federally Insured Credit Unions**

SUBJECT: **New Homeownership Counseling and Consumer Protection Requirements from CFPB**

ENCL: **(1) 2013 Home Ownership and Equity Protection Act (HOEPA) Rule – Small Entity Compliance Guide**
(2) NCUA Dodd-Frank Act HOEPA Loans Summary

ACTION: **Compliance Required by January 10, 2014**

Dear Board of Directors and Chief Executive Officer:

Effective January 10, 2014, you must comply with the new Home Ownership and Equity Protection Act (HOEPA) Rule from the Consumer Financial Protection Bureau (CFPB). The rule addresses two distinct subject matters – **new homeownership counseling requirements unrelated to HOEPA (or high-cost) loans and new consumer protections for HOEPA loans**. Under the rule, if on or after January 10, 2014:

1) Your credit union makes any federally related mortgage loan (whether or not it is a high-cost mortgage), including open-end and closed-end credit, you must provide a written list of homeownership counseling organizations to applicants within three days of the application;
2) Your credit union makes mortgage loans to first-time borrowers that permit negative amortization (whether or not it is a high-cost mortgage), you must confirm that these first-time borrowers have received homeownership counseling before consummation; or
3) Your credit union makes high-cost mortgages or open-end credit secured by a consumer's principal dwelling, you must comply with new HOEPA consumer protections and homeownership counseling requirements.

Regulatory Tips: Even if you have not made any high-cost mortgages in the past, you must verify whether your new mortgages are exempt from the new "high-cost" thresholds in CFPB's amended HOEPA rule.

Also, even if you don't make any high-cost mortgages under the new coverage thresholds, there are still homeownership counseling elements of the HOEPA rule with which you must comply.

The effective date for the HOEPA rule is January 10, 2014.

Background

HOEPA amended the Truth in Lending Act (TILA) to address abusive practices in refinancing first mortgages and granting home equity mortgage loans with high interest rates or high fees. HOEPA did *not* apply to purchase-money mortgages or reverse mortgages, but covered other closed-end mortgage credit, including refinances and closed-end home equity loans. HOEPA coverage was generally triggered when a loan's annual percentage rate (APR) exceeded comparable Treasury securities by specified thresholds for applicable loan types or when points and fees exceeded 8 percent of the total loan amount or an established dollar threshold.

Loans meeting the HOEPA coverage tests are subject to special pre-closing disclosure requirements and restrictions on prepayment penalties and loan terms, as well as regulated lender practices, such as a prohibition on extending credit without regard to a consumer's ability to repay the loan. HOEPA permits consumers to obtain damages for and void loans that include prohibited finance charges and fees. HOEPA also increased liability to purchasers of high-cost mortgages. The provisions of HOEPA were implemented in Section 32 of TILA's Regulation Z (12 CFR § 1026.32).[1]

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) expanded HOEPA coverage to purchase-money mortgage loans and home equity lines of credit (HELOCs) and added protections for high-cost mortgages, including a requirement that borrowers receive homeownership counseling before obtaining a high-cost mortgage. Additionally, Dodd-Frank requires or encourages consumers to obtain homeownership counseling for other types of loans.

On January 10, 2013, CFPB issued rules amending Regulation X (Real Estate Settlement Procedures Act, 12 CFR Part 1024) and Regulation Z (TILA, 12 CFR Part 1026) to implement these new Dodd-Frank HOEPA and homeownership counseling provisions.

I. Homeownership Counseling Provisions Unrelated to HOEPA Loans

Which Loans are Covered and What Counseling Information is Required?

The HOEPA rule contains homeownership counseling requirements for federally related mortgage loans, and loans to first-time borrowers that permit negative amortization, whether or not they are high-cost loans.

Federally Related Mortgage Loans

The rule requires that for federally related mortgage loans, within three days of receipt of an application by your credit union, **you must provide the applicant with a list of**

[1] Loans meeting the HOEPA coverage tests are commonly known as "HOEPA loans," "Section 32 loans," or "high-cost mortgages."

homeownership counseling organizations that provide relevant counseling services in the loan applicant's location.[2]

The term "federally related mortgage" is defined as a loan secured by a dwelling and includes purchase-money and non-purchase-money closed-end credit and HELOCs.[3] It does *not* include reverse mortgages and loans for timeshares.

The list provided to applicants must include 10 U.S. Department of Housing and Urban Development (HUD) approved homeownership counseling agencies closest to the applicant's location. The HOEPA rule specifies two methods for obtaining the list: 1) using a tool developed and maintained by CFPB on its website and 2) using data made available by CFPB or HUD.[4] In addition, the list must include certain explanatory text indicating that the applicant can find other approved counseling agencies by contacting CFPB or HUD.[5]

If there is more than one applicant, you may provide the list to the applicant with primary responsibility for the loan. If you do not provide the list in person, you must mail or deliver it by other means, including electronically, subject to the E-SIGN Act.

If there is more than one lender, only one list is required.

Unless otherwise prohibited, you may provide the list with other required disclosures.

After providing the list, it is up to consumers to decide if they want to get counseling; the rule does not require them to do so.

You do *not* need to provide the list if, before the end of the three business days, the application is denied or withdrawn.

Negative Amortization Loans

Before making a mortgage loan to a first-time borrower that permits negative amortization, you must confirm the borrower has received homeownership counseling. This requirement applies to most types of closed-end, dwelling-secured loans that allow for negative amortization. The required counseling must be provided by a federally certified or approved homeownership counselor. You cannot direct a member to choose a particular homeownership counseling organization.

Although you cannot make the loan before receiving confirmation of counseling, you may engage in other activities, such as processing the loan application or ordering an appraisal or title search.

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[2] This requirement is implemented in Regulation X, 12 C.F.R. § 1024.20.
[3] See 12 U.S.C. 2602; 12 CFR § 1024.2(b).
[4] CFPB Bulletin 2013-13 (November 8, 2013): http://www.consumerfinance.gov/find-a-housing-counselor.
[5] 78 F.R. 68343 (November 14, 2013) (Interpretive Final Rule).

II. High-Cost Mortgages Provisions

Which Loans are Covered?

The HOEPA rule expands the types of loans that might be subject to HOEPA coverage to include purchase-money mortgage loans and HELOCs, in addition to refinancings and closed-end home equity loans with high rates or high fees. Accordingly, the term "high-cost mortgage" now includes both a closed-end credit transaction and an open-end credit plan secured by the consumer's principal dwelling.[6]

Most types of mortgage loans secured by a consumer's principal dwelling are potentially subject to HOEPA coverage, including purchase-money mortgages, refinances, closed-end home equity loans, and open-end credit plans (home equity lines of credit or HELOCs).

Construction loans, reverse mortgages, and loans made by a Housing Finance Agency or through the U.S. Department of Agriculture (USDA) Rural Housing Service Section 502 Direct Loan Program are, in certain cases, exempted from HOEPA coverage.[7]

Three HOEPA Coverage Tests

The HOEPA rule revises the coverage tests for whether a loan is a "high-cost mortgage." A mortgage loan that meets the criteria of any one of the following three coverage tests is a high-cost mortgage for purposes of the HOEPA rule:

1. APR Coverage Test

A loan or credit transaction is a high-cost mortgage if the APR exceeds the average prime offer rate (APOR)[8] for a comparable transaction by more than:

- 6.5 percent for first lien mortgage loans;
- 8.5 percent for first lien mortgage loans less than $50,000 and secured by a dwelling that is personal property (including manufactured homes or recreational vehicles titled as personal property); or
- 8.5 percent for junior lien mortgage loans.

The APR for HOEPA coverage is calculated differently than the APR disclosed in TILA disclosures:

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[6] For purposes of determining coverage under 12 C.F.R. § 1026.32, the HOEPA rule clarifies that 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.

[7] The exemption for construction loans applies only to loans that finance the initial construction of a new dwelling. The exemptions for Housing Finance Agency and USDA loans do *not* apply to loans guaranteed or insured by these organizations.

[8] See http://www.ffiec.gov/ratespread/aportables.htm for a listing of APOR tables.

For fixed-rate loans, you calculate the APR for HOEPA coverage using the interest rate in effect on the date you set the interest rate for the loan.

For variable-rate loans, you use the greater of the introductory rate, if any, or the fully indexed rate. The fully indexed rate is the interest rate that results from adding the maximum allowable margin at any time during the term of the loan to the value of the index rate in effect on the date you set the interest rate for the loan. If the interest rate might vary other than according to an index, such as in a step-rate loan, use the maximum rate the loan applicant might pay during the loan term.

2. Points-and-Fees Coverage Test

A transaction is a high-cost mortgage if the total points and fees paid in connection with the loan exceed:

- 5 percent of the total loan amount if the loan amount is $20,000 or more; or
- For loans less than $20,000, the lesser of:
    - 8 percent of the total loan amount or
    - $1,000.[9]

To calculate the points and fees for *closed-end loans*, use the same general approach you would use under CFPB's Ability to Repay/Qualified Mortgage Rule (ATR/QM Rule).[10] The approach is described in pages 37-41 of the Ability to Repay and Qualified Mortgage Rule Small Entity Compliance Guide.

To calculate the points and fees for *HELOCs*, use the same general approach for calculating points and fees for closed-end loans, but include participation fees payable at or before account opening and fees members pay for drawing on their HELOC, if applicable.[11]

3. Prepayment Penalty Coverage Test[12]

A transaction is a high-cost mortgage if under the terms of the loan contract or open-end credit agreement, the creditor can charge a prepayment penalty:

- More than 36 months after consummation or account opening, or
- Greater than 2 percent of the amount prepaid.

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[9] The $1,000 and $20,000 figures will be adjusted annually for inflation. CFPB will publish the updated figures each year in the official staff commentary to Regulation Z.
[10] 78 F.R. 6407 (January 30, 2013), as amended.
[11] If your credit union charges a member a fee for drawing on a HELOC, you should assume the member will draw on the HELOC at least once.
[12] Federal credit unions are prohibited from charging prepayment penalties on any loan. 12 U.S.C. 1757(5)(A)(viii).

The prepayment penalty coverage test caps a prepayment penalty that state-chartered credit unions may charge on a high-cost mortgage to 2 percent of any prepayment amount or the time period during which a prepayment penalty could be charged to 36 months after consummation or account opening. Any amount in excess of the 2 percent cap or time period beyond 36 months is prohibited under the HOEPA rule.

What are the Consumer Protection Requirements for HOEPA Loans?

The HOEPA rule provides consumer protections for high-cost mortgages that require you to give additional disclosures, avoid certain loan terms, and ensure the consumer receives additional protections, including homeownership counseling.

New Specific Disclosure Requirements

A creditor must provide a written disclosure to the consumer at least three business days before a loan closing or account opening of a high-cost mortgage. The rule requires that the disclosure contain new specific information and wording about the loan.[13] The disclosure must:

- Inform the member that the loan is not effective until the transaction is closed or the account is opened;
- Explain the consequences of defaults;
- Disclose loan terms, such as APR, amount borrowed, and monthly payments; and
- In the case of variable-rate loans, explain the maximum monthly payment that might be required for a variable-rate loan.

New Restrictions on Loan Terms

The HOEPA rule restricts or prohibits risky loan features for high-cost mortgages.

Balloon payments are generally prohibited, unless:

- The loan payment schedule is adjusted to accommodate a member's seasonal or irregular income;
- The loan is a bridge loan with a term of 12 months or less to finance a new home purchase for a member selling an existing home; or
- Your credit union serves a predominantly rural or underserved area and the loan complies with the ATR/QM Rule. These terms differ from NCUA definitions of "rural" and "underserved areas" for chartering purposes. Credit unions may rely as a safe harbor on the list of counties published by CFPB to determine whether a county qualifies as rural or underserved for a particular calendar year.[14]

[13] The required wording for the disclosure is found in 12 CFR § 1026.32(c). Appendix H to Regulation Z also contains sample disclosures.
[14] CFPB placed a list of rural and underserved counties at http://www.consumerfinance.gov/blog/final-list-of-rural-and-or-underserved-counties-for-use-in-2013/.

Prepayment penalties are prohibited for high-cost mortgages.

Due-on-Demand features that allow for acceleration in high-cost mortgages are permitted only where:

- A member commits fraud or makes a material misrepresentation in connection with the loan;
- A member defaults on payment; or
- A member's action adversely affects your credit union's security interest.

Creditors and mortgage brokers may not recommend default on an existing loan for it to be refinanced by a high-cost mortgage. Creditors, servicers, and their assignees cannot charge a fee to modify, defer, renew, extend, or amend a high-cost mortgage. Late fees are restricted to 4 percent of the past-due payment, and pyramiding of late fees is prohibited. Additionally, fees for providing a payoff statement are generally prohibited.

You cannot finance points and fees on high-cost mortgages, but you can finance closing charges excluded from the definition of points and fees, such as bona fide third-party charges.

Finally, you cannot purposely structure a loan to evade HOEPA coverage.

New Ability-to-Repay Requirement

The HOEPA rule requires you to determine a member's ability to repay a high-cost mortgage before closing a loan or opening an account. For closed-end, high-cost HOEPA loans, you must comply with the ATR/QM rule. Because the ATR/QM rule does not apply to HELOCs, the HOEPA rule requires that you consider a member's:

- Current and reasonably expected income or assets; and
- Current obligations, including any mortgage-related obligations such as property taxes, required insurance premiums, community association fees, ground rent, and lease payments.

New Written Certification of Homeownership Counseling Requirement

Before making a high-cost mortgage, you must receive written certification from an unaffiliated, certified or approved counselor that a member received counseling on the advisability of the HOEPA loan. A member may not obtain counseling until after receiving the initial good faith estimate on a closed-end transaction or the initial HELOC disclosures required by Regulation Z. You cannot direct a member to a particular homeownership counseling organization.

A member may pay a bona fide third-party counseling fee, and you may finance the fee. You may also pay the fee, but you cannot condition payment on loan closing or account opening. You may confirm the counseling before paying the fee.

However, if a member withdraws the loan application, you may not condition the fee payment on receipt of the counseling certification.

Continuing HOEPA Protections

Regulation Z prohibits certain loan terms for high-cost mortgages, and the HOEPA rule left these prohibitions unchanged. The prohibitions are:

- Permitting negative amortizations;
- Permitting a payment schedule that consolidates more than two periodic payments and pays them in advance from the loan proceeds;
- Increasing the interest rate after a default;
- In the case of acceleration as a result of a default in payment, calculating a refund of interest in a manner less favorable to the member than the actuarial method;
- Paying a contractor under a home improvement contract from the proceeds of a high-cost mortgage;
- Selling a high-cost mortgage on the secondary market without providing a high-cost mortgage notice to the assignee; and
- Refinancing any high-cost mortgage into another high-cost mortgage within one year after extending credit, unless the refinancing is in a member's interest.

What Other Resources Are Available?

In addition to the referenced enclosures on the title page of this document, other resources are available.

The full text of the HOEPA rule published in the Federal Register is available at: https://www.federalregister.gov/articles/2013/01/31/2013-00740/high-cost-mortgage-and-homeownership-counseling-amendments-to-the-truth-in-lending-act-regulation-z.

CFPB resources to help you understand the HOEPA rule and its implications, information about proposed and subsequent adjustments to the rule,[15] and compliance materials are available at: http://www.consumerfinance.gov/regulations/high-cost-mortgage-and-homeownership-counseling-amendments-to-regulation-z-and-homeownership-counseling-amendments-to-regulation-x/.

Access to a publicly available, machine-readable housing counseling agency dataset generated by HUD can be found at http://data.hud.gov/index.html.

[15] On September 13, 2013, the CFPB clarified and revised the definition of points and fees for purposes of the high-cost mortgage points and fees threshold. On October 15, 2013, the CFPB clarified the specific disclosures that must be provided before counseling for high-cost mortgages can occur. Additionally, on November 8, 2013, the CFPB provided data instructions for a homeownership counseling list for larger institutions and an online tool for smaller institutions.

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

Sincerely,

Debbie Matz
Chairman