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BUREAU OF CONSUMER FINANCIAL PROTECTION

12 CFR Part 1026

Docket No. CFPB-2014-0009

RIN 3170-AA43

Amendments to the 2013 Mortgage Rules under the Truth in Lending Act (Regulation Z)

AGENCY: Bureau of Consumer Financial Protection.

ACTION: Proposed rule with request for public comment.

SUMMARY: The Bureau of Consumer Financial Protection (Bureau) proposes amendments to certain mortgage rules issued in 2013. The proposed rule would provide an alternative small servicer definition for nonprofit entities that meet certain requirements, amend the existing exemption from the ability-to-repay rule for nonprofit entities that meet certain requirements, and provide a limited cure mechanism for the points and fees limit that applies to qualified mortgages.

DATES: Comments regarding the proposed amendments to 12 CFR §§ 1026.41(e)(4), 1026.43(a)(3), and 1026.43(e)(3) must be received on or before **[INSERT DATE 30 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]**. For the requests for comment regarding correction or cure of debt-to-income ratio overages and the credit extension limit for the small creditor definition, comments must be received on or before **[INSERT DATE 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: You may submit comments, identified by Docket No. CFPB-2014-0009 or RIN 3170-AA34, by any of the following methods:

- *Electronic*: http://www.regulations.gov. Follow the instructions for submitting comments.
- *Mail/Hand Delivery/Courier:* Monica Jackson, Office of the Executive Secretary, Consumer Financial Protection Bureau, 1700 G Street, NW, Washington, DC 20552.

Instructions: All submissions should include the agency name and docket number or Regulatory Information Number (RIN) for this rulemaking. Because paper mail in the Washington, DC area and at the Bureau is subject to delay, commenters are encouraged to submit comments electronically. In general, all comments received will be posted without change to http://www.regulations.gov. In addition, comments will be available for public inspection and copying at 1700 G Street, NW, Washington, DC 20552, on official business days between the hours of 10 a.m. and 5 p.m. Eastern Time. You can make an appointment to inspect the documents by telephoning (202) 435-7275.

All comments, including attachments and other supporting materials, will become part of the public record and subject to public disclosure. Sensitive personal information, such as account numbers or social security numbers, should not be included. Comments generally will not be edited to remove any identifying or contact information.

FOR FURTHER INFORMATION CONTACT: Pedro De Oliveira, Counsel; William R. Corbett, Nicholas Hluchyj, and Priscilla Walton-Fein, Senior Counsels, Office of Regulations, at (202) 435-7700.

SUPPLEMENTARY INFORMATION:

I. Summary of Proposed Rule

In January 2013, the Bureau issued several final rules concerning mortgage markets in the United States (2013 Title XIV Final Rules), pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Public Law No. 111-203, 124 Stat. 1376 (2010).[1] The Bureau clarified and revised those rules through notice and comment rulemaking during the summer and fall of 2013. The purpose of those updates was to address important questions raised by industry, consumer groups, or other stakeholders. The Bureau is now proposing several additional amendments to the 2013 Title XIV Final Rules to revise regulatory provisions and official interpretations primarily relating to the Regulation Z ability-to-repay/qualified mortgage requirements and servicing rules, as well as seeking comment on additional issues. The Bureau expects to issue additional proposals to address other topics relating to the 2013 Title XIV Final Rules, such as the definition of "rural and underserved" for purposes of certain mortgage provisions affecting small creditors as discussed further below.

Specifically, the Bureau is proposing three amendments to the 2013 Title XIV Final Rules:

- To provide an alternative definition of the term "small servicer," that would apply to certain nonprofit entities that service for a fee loans on behalf of other nonprofit chapters of the same organization. Although the Bureau is proposing this change

[1] Specifically, on January 10, 2013, the Bureau issued Escrow Requirements Under the Truth in Lending Act (Regulation Z), 78 FR 4725 (Jan. 22, 2013) (2013 Escrows Final Rule), High-Cost Mortgage and Homeownership Counseling Amendments to the Truth in Lending Act (Regulation Z) and Homeownership Counseling Amendments to the Real Estate Settlement Procedures Act (Regulation X), 78 FR 6855 (Jan. 31, 2013) (2013 HOEPA Final Rule), and Ability to Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 FR 6407 (Jan. 30, 2013) (January 2013 ATR Final Rule). The Bureau concurrently issued a proposal to amend the January 2013 ATR Final Rule, which was finalized on May 29, 2013. *See* 78 FR 6621 (Jan. 30, 2013) (January 2013 ATR Proposal) and 78 FR 35429 (June 12, 2013) (May 2013 ATR Final Rule). On January 17, 2013, the Bureau issued the Real Estate Settlement Procedures Act (Regulation X) and Truth in Lending Act (Regulation Z) Mortgage Servicing Final Rules, 78 FR 10901 (Feb. 14, 2013) (Regulation Z) and 78 FR 10695 (Feb. 14, 2013) (Regulation X) (2013 Mortgage Servicing Final Rules). On January 18, 2013, the Bureau issued the Disclosure and Delivery Requirements for Copies of Appraisals and Other Written Valuations Under the Equal Credit Opportunity Act (Regulation B), 78 FR 7215 (Jan. 31, 2013) (2013 ECOA Valuations Final Rule) and, jointly with other agencies, issued Appraisals for Higher-Priced Mortgage Loans (Regulation Z), 78 FR 10367 (Feb. 13, 2013) (2013 Interagency Appraisals Final Rule). On January 20, 2013, the Bureau issued the Loan Originator Compensation Requirements under the Truth in Lending Act (Regulation Z), 78 FR 11279 (Feb. 15, 2013) (2013 Loan Originator Final Rule).

in Regulation Z, the change will also affect several provisions of Regulation X, which cross-reference the Regulation Z small servicer exemption.

- To amend the Regulation Z ability-to-repay requirements to provide that certain interest-free, contingent subordinate liens originated by nonprofit creditors will not be counted towards the credit extension limit that applies to the nonprofit exemption from the ability-to-repay requirements.
- To provide a limited, post-consummation cure mechanism for loans that are originated with the good faith expectation of qualified mortgage status but that actually exceed the points and fees limit for qualified mortgages.

In addition to providing specific proposals on these issues, the Bureau is seeking comment on two additional topics:

- Whether and how to provide a limited, post-consummation cure or correction provision for loans that are originated with the good faith expectation of qualified mortgage status but that actually exceed the 43-percent debt-to-income ratio limit that applies to certain qualified mortgages.
- Feedback and data from smaller creditors regarding implementation of certain provisions in the 2013 Title XIV Final Rules that are tailored to account for small creditor operations and how their origination activities have changed in light of the new rules.

II. Background

A. Title XIV Rulemakings under the Dodd-Frank Act

In response to an unprecedented cycle of expansion and contraction in the mortgage market that sparked the most severe U.S. recession since the Great Depression, Congress passed the Dodd-Frank Act, which was signed into law on July 21, 2010. In the Dodd-Frank Act, Congress established the Bureau and generally consolidated the rulemaking authority for Federal consumer financial laws, including the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA), in the Bureau.[2] At the same time, Congress significantly amended the statutory requirements governing mortgage practices, with the intent to restrict the practices that contributed to and exacerbated the crisis.[3] Under the statute, most of these new requirements would have taken effect automatically on January 21, 2013, if the Bureau had not issued implementing regulations by that date.[4] To avoid uncertainty and potential disruption in the national mortgage market at a time of economic vulnerability, the Bureau issued several final rules in a span of less than two weeks in January 2013 to implement these new statutory provisions and provide for an orderly transition.

On January 10, 2013, the Bureau issued the 2013 Escrows Final Rule, the January 2013 ATR Final Rule, and the 2013 HOEPA Final Rule. 78 FR 4725 (Jan. 22, 2013); 78 FR 6407 (Jan. 30, 2013); 78 FR 6855 (Jan. 31, 2013). On January 17, 2013, the Bureau issued the 2013 Mortgage Servicing Final Rules. 78 FR 10695 (Feb. 14, 2013); 78 FR 10901 (Feb. 14, 2013). On January 18, 2013, the Bureau issued the 2013 ECOA Valuations Final Rule and, jointly with other agencies, the 2013 Interagency Appraisals Final Rule. 78 FR 7215 (Jan. 31, 2013); 78 FR 10367 (Feb. 13, 2013). On January 20, 2013, the Bureau issued the 2013 Loan Originator Final

[2] *See, e.g.*, sections 1011 and 1021 of the Dodd-Frank Act, 12 U.S.C. 5491 and 5511 (establishing and setting forth the purpose, objectives, and functions of the Bureau); section 1061 of the Dodd-Frank Act, 12 U.S.C. 5581 (consolidating certain rulemaking authority for Federal consumer financial laws in the Bureau); section 1100A of the Dodd-Frank Act (codified in scattered sections of 15 U.S.C.) (similarly consolidating certain rulemaking authority in the Bureau). *But see* Section 1029 of the Dodd-Frank Act, 12 U.S.C. 5519 (subject to certain exceptions, excluding from the Bureau's authority any rulemaking authority over a motor vehicle dealer that is predominantly engaged in the sale and servicing of motor vehicles, the leasing and servicing of motor vehicles, or both).

[3] *See* title XIV of the Dodd-Frank Act, Public Law 111-203, 124 Stat. 1376 (2010) (codified in scattered sections of 12 U.S.C., 15 U.S.C., and 42 U.S.C.).

[4] *See* section 1400(c) of the Dodd-Frank Act, 15 U.S.C. 1601 note.

Rule. 78 FR 11279 (Feb. 15, 2013).[5] Pursuant to the Dodd-Frank Act, which permitted a maximum of one year for implementation, most of these rules became effective on January 10, 2014.

Concurrent with the January 2013 ATR Final Rule, on January 10, 2013, the Bureau issued proposed amendments to the rule (*i.e.*, the January 2013 ATR Proposal), which the Bureau finalized on May 29, 2013 (*i.e.*, the May 2013 ATR Final Rule). 78 FR 6621 (Jan. 30, 2013); 78 FR 35429 (June 12, 2013). The Bureau issued additional corrections and clarifications to the 2013 Mortgage Servicing Final Rules and the May 2013 ATR Final Rule in the summer and fall of 2013.[6]

B. Implementation Plan for New Mortgage Rules

On February 13, 2013, the Bureau announced an initiative to support implementation of its new mortgage rules (the Implementation Plan),[7] under which the Bureau would work with the mortgage industry and other stakeholders to ensure that the new rules could be implemented accurately and expeditiously. The Implementation Plan included: (1) coordination with other agencies, including the development of consistent, updated examination procedures; (2) publication of plain-language guides to the new rules; (3) publication of additional corrections and clarifications of the new rules, as needed; (4) publication of readiness guides for the new rules; and (5) education of consumers on the new rules.

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[5] Each of these rules was published in the **Federal Register** shortly after issuance.

[6] 78 FR 44685 (July 24, 2013) (clarifying which mortgages to consider in determining small servicer status and the application of the small servicer exemption with regard to servicer/affiliate and master servicer/subservicer relationships); 78 FR 45842 (July 30, 2013); 78 FR 60381 (Oct. 1, 2013) (revising exceptions available to small creditors operating predominantly in ‘‘rural’’ or ‘‘underserved’’ areas); 78 FR 62993 (Oct. 23, 2013) (clarifying proper compliance regarding servicing requirements when a consumer is in bankruptcy or sends a cease communication request under the Fair Debt Collection Practice Act).

[7] Press Release, Consumer Financial Protection Bureau, *Consumer Financial Protection Bureau Lays Out Implementation Plan for New Mortgage Rules* (Feb. 13, 2013), *available at* http://www.consumerfinance.gov/newsroom/consumer-financial-protection-bureau-lays-out-implementation-plan-for-new-mortgage-rules/.

This proposal concerns additional revisions to the new rules. The purpose of these updates is to address important questions raised by industry, consumer groups, or other stakeholders. As discussed below, the Bureau contemplates issuing additional updates on additional topics.

III. Legal Authority

The Bureau is issuing this proposed rule pursuant to its authority under TILA, RESPA, and the Dodd-Frank Act. Section 1061 of the Dodd-Frank Act transferred to the Bureau the "consumer financial protection functions" previously vested in certain other Federal agencies, including the Board of Governors of the Federal Reserve System (Board). The term "consumer financial protection function" is defined to include "all authority to prescribe rules or issue orders or guidelines pursuant to any Federal consumer financial law, including performing appropriate functions to promulgate and review such rules, orders, and guidelines. Section 1061 of the Dodd-Frank Act also transferred to the Bureau all of the Department of Housing and Urban Development's (HUD) consumer protection functions relating to RESPA. Title X of the Dodd-Frank Act, including section 1061 of the Dodd-Frank Act, along with TILA, RESPA, and certain subtitles and provisions of title XIV of the Dodd-Frank Act, are Federal consumer financial laws.[8]

A. TILA

Section 105(a) of TILA authorizes the Bureau to prescribe regulations to carry out the purposes of TILA. 15 U.S.C. 1604(a). Under section 105(a), such regulations may contain such

[8] Dodd-Frank Act section 1002(14), 12 U.S.C. 5481(14) (defining "Federal consumer financial law" to include the "enumerated consumer laws," the provisions of title X of the Dodd-Frank Act, and the laws for which authorities are transferred under title X subtitles F and H of the Dodd-Frank Act); Dodd-Frank Act section 1002(12), 12 U.S.C. 5481(12) (defining "enumerated consumer laws" to include TILA); Dodd-Frank section 1400(b), 12 U.S.C. 5481(12) note (defining "enumerated consumer laws" to include certain subtitles and provisions of Dodd-Frank Act title XIV); Dodd-Frank Act section 1061(b)(7), 12 U.S.C. 5581(b)(7) (transferring to the Bureau all of HUD's consumer protection functions relating to RESPA).

additional requirements, classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for all or any class of transactions, as in the judgment of the Bureau are necessary or proper to effectuate the purposes of TILA, to prevent circumvention or evasion thereof, or to facilitate compliance therewith. A purpose of TILA is "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit." TILA section 102(a), 15 U.S.C. 1601(a). In particular, it is a purpose of TILA section 129C, as added by the Dodd-Frank Act, to assure that consumers are offered and receive residential mortgage loans on terms that reasonably reflect their ability to repay the loans and that are understandable and not unfair, deceptive, and abusive. 15 U.S.C. 1639b(a)(2).

Section 105(f) of TILA authorizes the Bureau to exempt from all or part of TILA a class of transactions if the Bureau determines that TILA coverage does not provide a meaningful benefit to consumers in the form of useful information or protection. 15 U.S.C. 1604(f)(1). That determination must consider:

- The loan amount and whether TILA's provisions "provide a benefit to the consumers who are parties to such transactions";
- The extent to which TILA requirements "complicate, hinder, or make more expensive the credit process";
- The borrowers' "status," including their "related financial arrangements," their financial sophistication relative to the type of transaction, and the importance to the borrowers of the credit, related supporting property, and TILA coverage;
- Whether the loan is secured by the consumer's principal residence; and
- Whether consumer protection would be undermined by such an exemption.

15 U.S.C. 1604(f)(2).

TILA section 129C(b)(3)(B)(i) provides the Bureau with authority to prescribe regulations that revise, add to, or subtract from the criteria that define a qualified mortgage upon a finding that such regulations are: necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of the ability-to-repay requirements; necessary and appropriate to effectuate the purposes of the ability-to-repay and residential mortgage loan origination requirements; to prevent circumvention or evasion thereof; or to facilitate compliance with TILA sections 129B and 129C. 15 U.S.C. 1639c(b)(3)(B)(i). In addition, TILA section 129C(b)(3)(A) requires the Bureau to prescribe regulations to carry out such purposes. 15 U.S.C. 1639c(b)(3)(A).

B. RESPA

Section 19(a) of RESPA authorizes the Bureau to prescribe such rules and regulations, to make such interpretations, and to grant such reasonable exemptions for classes of transactions, as may be necessary to achieve the purposes of RESPA, which include RESPA's consumer protection purposes. 12 U.S.C. 2617(a). In addition, section 6(j)(3) of RESPA authorizes the Bureau to establish any requirements necessary to carry out section 6 of RESPA, and section 6(k)(1)(E) of RESPA authorizes the Bureau to prescribe regulations that are appropriate to carry out RESPA's consumer protection purposes. 12 U.S.C. 2605(j)(3) and (k)(1)(E). The consumer protection purposes of RESPA include responding to borrower requests and complaints in a timely manner, maintaining and providing accurate information, helping borrowers avoid unwarranted or unnecessary costs and fees, and facilitating review for foreclosure avoidance options.

C. The Dodd-Frank Act

Section 1405(b) of the Dodd-Frank Act provides that, "in order to improve consumer awareness and understanding of transactions involving residential mortgage loans through the use of disclosures," the Bureau may exempt from disclosure requirements, "in whole or in part . . . any class of residential mortgage loans" if the Bureau determines that such exemption "is in the interest of consumers and in the public interest." 15 U.S.C. 1601 note.[9] Notably, the authority granted by section 1405(b) applies to "disclosure requirements" generally, and is not limited to a specific statute or statutes. Accordingly, Dodd-Frank Act section 1405(b) is a broad source of authority for exemptions from the disclosure requirements of TILA and RESPA.

Moreover, section 1022(b)(1) of the Dodd-Frank Act authorizes the Bureau to prescribe rules "as may be necessary or appropriate to enable the Bureau to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof." 12 U.S.C. 5512(b)(1). Accordingly, the Bureau is exercising its authority under Dodd-Frank Act section 1022(b) to propose rules that carry out the purposes and objectives of TILA, RESPA, title X of the Dodd-Frank Act, and certain enumerated subtitles and provisions of title XIV of the Dodd-Frank Act, and to prevent evasion of those laws.

The Bureau is proposing to amend rules that implement certain Dodd-Frank Act provisions. In particular, the Bureau is proposing to amend provisions of Regulation Z (and, by reference, Regulation X) adopted by the 2013 Mortgage Servicing Final Rules (including July 2013 amendments thereto), the January 2013 ATR Final Rule, and the May 2013 ATR Final Rule.

IV. Proposed Effective Date

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[9]"Residential mortgage loan" is generally defined as any consumer credit transaction (other than open-end credit plans) that is secured by a mortgage (or equivalent security interest) on "a dwelling or on residential real property that includes a dwelling" (except, in certain instances, timeshare plans). 15 U.S.C. 1602(cc)(5).

The Bureau proposes that all of the changes proposed herein take effect thirty days after publication of a final rule in the **Federal Register**. The proposed changes would expand exemptions and provide relief from regulatory requirements; therefore the Bureau believes an effective date of 30 days after publication may be appropriate. The Bureau seeks comment on whether the proposed effective date is appropriate, or whether the Bureau should adopt an alternative effective date.

V. Section-by-Section Analysis

Section 1026.41 Periodic Statements for Residential Mortgage Loans

41(e) Exemptions

41(e)(4) Small Servicers

The Bureau is proposing to revise the scope of the exemption for small servicers that is set forth in § 1026.41 of Regulation Z and incorporated by cross-reference in certain provisions of Regulation X. The proposal would add an alternative definition of small servicer which would apply to certain nonprofit entities that service for a fee only loans for which the servicer or an associated nonprofit entity is the creditor.

The Bureau's 2013 Mortgage Servicing Final Rules exempt small servicers from certain mortgage servicing requirements. Specifically, Regulation Z exempts small servicers, defined in § 1026.41(e)(4)(ii), from the requirement to provide periodic statements for residential mortgage loans.[10] Regulation X incorporates this same definition by reference to § 1026.41(e)(4) and thereby exempts small servicers from: (1) certain requirements relating to obtaining force-placed insurance,[11] (2) the general servicing policies, procedures, and requirements,[12] and (3) certain

[10] 12 CFR 1026.41(e) (requiring delivery each billing cycle of a periodic statement, with specific content and form). For loans serviced by a small servicer, a creditor or assignee is also exempt from the Regulation Z periodic statement requirements. 12 CFR 1026.41(e)(4)(i).
[11] 12 CFR 1024.17(k)(5) (prohibiting purchase of force-placed insurance in certain circumstances).

requirements and restrictions relating to communicating with borrowers about, and evaluation of applications for, loss mitigation options.[13]

Current § 1026.41(e)(4)(ii) defines the term "small servicer" as a servicer that either: (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; or (B) is a Housing Finance Agency, as defined in 24 CFR 266.5. "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.* (BHCA).[14]

Generally, under § 1026.41(e)(4)(ii)(A), a servicer cannot be a small servicer if it services any loan for which the servicer or its affiliate is not the creditor or assignee. However, current § 1026.41(e)(4)(iii) excludes from consideration certain types of mortgage loans for purposes of 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; and (C) mortgage loans secured by consumers' interests in timeshare plans. In the 2013 Mortgage Servicing Final Rules, the Bureau concluded that a separate exemption for nonprofits was not necessary because the Bureau believed that nonprofits would likely fall within the small servicer exemption. *See* 78 FR 10695, 10720 (Feb. 14, 2013).

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[12] 12 CFR 1024.30(b)(1) (exempting small servicers from §§ 1024.38 through 41, except as otherwise provided under 41(j), as discussed in note 13, *infra*). Sections 1024.38 through 40 respectively impose general servicing policies, procedures, and requirements; early intervention requirements for delinquent borrowers; and policies and procedures to maintain continuity of contact with delinquent borrowers).

[13] *See* 12 CFR 1024.41 (loss mitigation procedures). Though exempt from most of the rule, small servicers are subject to the prohibition of foreclosure referral before the loan obligation is more than 120 days delinquent and may not make the first notice or filing for foreclosure if a borrower is performing pursuant to the terms of an agreement on a loss mitigation option. 12 CFR 1024.41(j).

[14] Under the BHCA, a company has "control" over another company if it (i) "directly or indirectly . . . owns, controls, or has power to vote 25 per centum or more of any class of voting securities" of the other company; (ii) "controls . . . the election of a majority of the directors or trustees" of the other company; or (iii) "directly or indirectly exercises a controlling influence over the management or policies" of the other company (based on a determination by the Board). 12 U.S.C. 1841(a)(2).

As part of the Bureau's Implementation Plan, the Bureau has learned that certain nonprofit entities may, for a fee, service loans for another nonprofit entity that is the creditor on the loan. The Bureau understands that, in some cases, these nonprofit entities are part of a larger association of nonprofits that are separately incorporated but operate under mutual contractual obligations to serve the same charitable mission, and that use a common name, trademark, or servicemark. These entities likely do not meet the definition of "affiliate" under the BHCA due to the limits imposed on nonprofits with respect to ownership and control. Accordingly, these nonprofits likely do not qualify for the small servicer exemption because they service, for a fee, loans on behalf of an entity that is not an affiliate as defined under the BHCA (and because the servicer is neither the creditor for, nor an assignee of, those loans).

The Bureau understands that groups of nonprofit entities that are associated with one another may consolidate servicing activities to achieve economies of scale necessary to service loans cost-effectively, and that such costs savings may reduce the cost of credit or enable the nonprofit to extend a greater number of loans overall. However, because of their corporate structures, such groups of nonprofit entities have a more difficult time than related for-profit servicers qualifying for the small servicer exemption. For the reasons discussed below, the Bureau believes that the ability of such nonprofit entities to consolidate servicing activities may be beneficial to consumers—*e.g.*, to the extent servicing cost savings are passed on to consumers and/or lead to increased credit availability—and may outweigh the consumer protections provided by the servicing rules to those consumers affected by this proposal.

Accordingly, the Bureau is proposing an alternative definition of small servicer that would apply to nonprofit entities that service loans on behalf of other nonprofits within a common network or group of nonprofit entities. Specifically, proposed § 1026.41(e)(4)(ii)(C) provides that a small servicer 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. Proposed § 1026.41(e)(4)(ii)(C)(*1*) provides that, for purposes of proposed § 1026.41(e)(4)(ii)(C), 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. *See* 26 U.S.C. 501(c)(3); 26 CFR 1.501(c)(3)-1. Proposed § 1026.41(e)(4)(ii)(C)(*2*) defines "associated nonprofit entities" to mean nonprofit entities that by agreement operate using a common name, trademark, or servicemark to further and support a common charitable mission or purpose.

The Bureau is also proposing technical changes to § 1026.41(e)(4)(iii), which addresses the timing of the small servicer determination and also excludes certain loans from the 5,000-loan limitation. The proposed changes would add language to the existing timing requirement to limit its application to the small servicer determination for purposes of § 1026.41(e)(4)(ii)(A) and insert a separate timing requirement for purposes of determining whether a nonprofit servicer is a small servicer pursuant to § 1026.41(e)(4)(ii)(C). Specifically, that requirement would provide that 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.

The Bureau is proposing technical changes to comment 41(e)(4)(ii)-2 in light of proposed § 1026.41(e)(4)(ii)(C). In addition, the Bureau is proposing to add a comment to parallel existing comment 41(e)(4)(ii)-2 (that addresses the requirements to be a small servicer under the existing definition in § 1026.41(e)(4)(ii)(A)). Specifically, new comment 41(e)(4)(ii)-4 would clarify that there are two elements to satisfying the nonprofit small creditor definition in proposed § 1026.41(e)(4)(ii)(C). First, the comment would clarify that 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, the comment would further explain that the 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). The comment would explain that 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 comment would provide two examples to demonstrate the application of the small servicer definition under § 1026.41(e)(4)(ii)(C).

The Bureau is also proposing to revise existing comment 41(e)(4)(iii)-3 to specify that it explains the application of § 1026.41(e)(4)(iii) to the small servicer determination under § 1026.41(e)(4)(ii)(A) specifically. As revised, comment 41(e)(4)(iii)-3 would explain that mortgage loans that are not considered pursuant to § 1026.41(e)(4)(iii) for purposes of the small servicer determination under § 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. The proposal would also make clarifying changes to the example provided in comment 41(e)(4)(iii)-3 and would move language in existing comment 41(e)(4)(iii)-3 regarding the limited role of voluntarily serviced mortgage loans to new proposed comment 41(e)(4)(iii)-5.

The Bureau is also proposing technical changes to comment 41(e)(4)(iii)-2 in light of proposed § 1026.41(e)(4)(ii)(C).

In addition, the Bureau is proposing a new comment 41(e)(4)(iii)-4 to explain the application of § 1026.41(e)(4)(iii) to the nonprofit small servicer determination under proposed § 1026.41(e)(4)(ii)(C) specifically. The proposed comment would explain that mortgage loans that are not considered pursuant to § 1026.41(e)(4)(iii) for purposes of the small servicer determination under § 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. The comment would provide an example of a nonprofit entity that services 5,400 mortgage loans. Of these mortgage loans, it 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 qualifies for the small servicer exemption pursuant to § 1026.41(e)(4)(ii)(C) with regard to all 5,400 mortgage loans it services.

The Bureau believes that nonprofit entities are an important source of credit, particularly for low- and moderate-income consumers. The Bureau understands that nonprofit entities, while they may operate under a common name, trademark, or servicemark, are not typically structured to meet the definition of affiliate under the BHCA. However, nonprofit entities derive less revenue than other creditors or servicers from their lending activities, and therefore the Bureau believes associated nonprofit entities may seek to coordinate activities—including loan servicing—as a means of achieving economies of scale.

Under the existing rule, a servicer qualifies for the small servicer exemption if it services for a fee a loan for which another entity is the creditor or assignee, so long as both entities are affiliates under the BHCA and the servicer and its affiliates together service 5,000 or fewer mortgage loans. Since nonprofit entities are not typically structured to meet the definition of affiliate under the BHCA, a nonprofit entity that services, for a fee, even a single loan of an associated nonprofit entity likely would not qualify as a small servicer under the current rule. The Bureau is proposing an alternative small servicer definition for nonprofits to permit associated nonprofit entities to enter into the type of servicing arrangements, such as consolidation of servicing activities, that are available to affiliates under the current rule.

The limitation in the current rule to BHCA affiliates may discourage consolidation of servicing among associated nonprofits, even though such consolidation may benefit consumers by increasing access to credit and reducing the cost of credit for low- and moderate-income consumers for whom nonprofits are an important source of credit. In addition, consolidating servicing in one entity within the associated nonprofit structure may enhance the nonprofit's ability to promptly credit payments, administer escrow account obligations, or handle error requests or other requirements under Regulations X and Z, which are applicable regardless of small servicer status. In addition, though small servicers are exempt from the requirements of §§ 1024.38 through 1024.40, as well as most of the loss mitigation provisions under § 1024.41, the Bureau believes that delinquent borrowers may nonetheless benefit from consolidated nonprofit servicers' enhanced ability to devote trained staff to their situation.

The Bureau is concerned that if nonprofit servicers are subject to all of the servicing rules, low- and moderate-income consumers may face increased costs or reduced access to credit. Although the Bureau believes the servicing rules provide important protections for consumers, the Bureau is concerned that these protections may not outweigh the risk of reduction in credit access for low- and moderate-income consumers served by nonprofit entities that qualify for the proposed § 1026.41(e)(4)(ii)(C) exemption. Furthermore, the Bureau believes these nonprofit entities, because of their scale and community-focused lending programs, already have incentives to provide high levels of customer contact and information—incentives that warrant exempting those servicers from complying with the periodic statement requirements under Regulation Z and certain requirements of Regulation X discussed above.

The Bureau has narrowly tailored the proposed small servicer definition for nonprofits to prevent evasion of the servicing rules. For example, the proposed definition contains restrictions on nonprofits and requires that a substantial relationship exist among the associated nonprofits to qualify for the exemption. As noted above, the definition would be limited to groups of nonprofits that share a common name, trademark, or servicemark to further and support a common charitable mission or purpose. The Bureau believes that requiring such commonality reduces the risk that the small servicer definition will be used to circumvent the servicing rules. However, the Bureau seeks comment on whether the proposed definition of "associated nonprofit entities" is appropriate.

The Bureau has further limited the scope of the proposed nonprofit small servicer definition to entities designated with an exemption under 501(c)(3) of the Internal Revenue

Code. As the Bureau noted in the January 2013 ATR Proposal, the Bureau believes that 501(c)(3)-designated entities face particular constraints on resources that other tax-exempt organizations may not. *See* 78 FR 6621, 6644-45 (Jan. 30, 2013). As a result, these entities may have fewer resources to comply with additional rules. In addition, tax-exempt status under section 501(c)(3) requires a formal determination by the government, in contrast to other types of tax-exempt status. Accordingly, limiting the proposed nonprofit small servicer provision to those entities with IRS tax exempt determinations for wholly charitable organizations may help to ensure that the nonprofit small servicer status is not used to evade the servicing rules. However, the Bureau solicits comment on whether limitation of the definition of "nonprofit entity" for purposes of § 1026.41(e)(4)(ii)(C) to entities with a tax exemption ruling or determination letter from the Internal Revenue Service under section 501(c)(3) of the Internal Revenue Code is appropriate. The Bureau also seeks comment on whether it is appropriate to include additional criteria regarding the nonprofit entity's activities or the loans' features or purposes, such as those in the nonprofit exemption from the ability to repay requirements in § 1026.43(a)(3)(v)(D) or in other statutory or regulatory schemes.

As noted above, the proposed alternative small servicer definition in § 1026.41(e)(4)(ii)(C) would apply to nonprofit entities that service 5,000 or fewer mortgage loans. The Bureau believes that it is necessary, in general, to limit the number of loans serviced by small servicers to prevent evasion of the servicing rules and because the Bureau believes that entities servicing more than 5,000 mortgage loans are of a sufficient size to comply with the full set of servicing rules. However, the proposed rule would apply that loan limitation to associated nonprofit entities differently than to affiliates. Specifically, the definition of small servicer in § 1026.41(e)(4)(ii)(A) counts towards the 5,000-loan limitation all loans serviced by the servicer together with all loans serviced by any affiliates. In contrast, the proposed rule for nonprofit entities would count towards the 5,000-loan limitation only the loans serviced by a given nonprofit entity (including loans it services on behalf of associated nonprofit entities), and would not consider loans serviced by associated nonprofit entities. As noted above, the Bureau is concerned that small servicers generally lack the ability to cost-effectively comply with the full set of servicing rules, a concern that is heightened in the context of nonprofit small servicers which derive less revenue than other creditors or servicers from their lending activities. Some nonprofits may consolidate servicing activities to achieve economies of scale across associated nonprofits. However, the Bureau is also concerned that other nonprofits may be structured differently and that for these nonprofit entities maintaining servicing at the individual nonprofit level may be more appropriate. For this reason, the Bureau does not believe it is appropriate to consider all loans serviced across the associated nonprofit enterprise towards the 5,000-loan limitation. The Bureau seeks comment on whether it is appropriate to count only loans serviced by a single nonprofit or whether the small servicer determination should be made based upon all loans serviced among a group of associated nonprofits.

The proposed exemption would also apply only to a nonprofit entity that services loans for which it or an associated nonprofit entity is the creditor. In contrast with the exemption under § 1026.41(e)(4)(ii)(A), the proposed exemption would not apply to a nonprofit entity that services loans for which it or an associated nonprofit entity is the assignee of the loans being serviced. The Bureau believes that nonprofit entities typically do not service loans for which an entity other than that nonprofit entity or an associated nonprofit is the creditor, nor does the Bureau believe that nonprofit entities typically take an assignment of a loan originated by an entity other than an associated nonprofit entity. Further, the Bureau is concerned that a rule that permits a nonprofit servicer to service for a fee loans that were originated by someone other than itself or an associated nonprofit entity while retaining the benefit of the exemption could be used to evade the servicing rules, particularly since the proposed rule would not consider loans serviced by associated nonprofit entities as counting towards the 5,000-loan limit. The Bureau seeks comment on whether limiting the exemption to loans for which the servicer or an associated nonprofit entity is the creditor is appropriate.

Legal Authority

The Bureau is proposing to exempt nonprofit small servicers from the periodic statement requirement under TILA section 128(f) pursuant to its authority under TILA section 105(a) and (f), and Dodd-Frank Act section 1405(b).

For the reasons discussed above, the Bureau believes the proposed exemption is necessary and proper under TILA section 105(a) to facilitate TILA compliance. The purpose of the periodic statement requirement is to ensure that consumers receive ongoing customer contact and account information. As discussed above, the Bureau believes that nonprofit entities that qualify for the exemption have incentives to provide ongoing consumer contact and account information that would exist absent a regulatory requirement to do so. The Bureau also believes that such nonprofits may consolidate servicing functions in an associated nonprofit entity to cost-effectively provide this high level of customer contact and otherwise comply with applicable regulatory requirements. As described above, the Bureau is concerned that the current rule may discourage consolidation of servicing functions. As a result, the current rule may result in nonprofits being unable to provide high-contact servicing or to comply with other applicable regulatory requirements due to the costs that would be imposed on each individual servicer. Accordingly, the Bureau believes the proposed nonprofit small servicer definition facilitates compliance with TILA by allowing nonprofit small servicers to consolidate servicing functions, without losing status as a small servicer, in order to cost-effectively service loans in compliance with applicable regulatory requirements.

In addition, consistent with TILA section 105(f) and in light of the factors in that provision, for a nonprofit entity servicing 5,000 or fewer loans, including those serviced on behalf of associated nonprofits, all of which that servicer or an associated nonprofit originated, the Bureau believes that requiring them to comply with the periodic statement requirement in TILA section 128(f) would not provide a meaningful benefit to consumers in the form of useful information or protection. The Bureau believes, as noted above, that these nonprofit servicers have incentives to provide consumers with necessary information, and that requiring provision of periodic statements would impose significant costs and burden. Specifically, the Bureau believes that the proposal will not complicate, hinder, or make more expensive the credit process—and is proper without regard to the amount of the loan, to the status of the consumer (including related financial arrangements, financial sophistication, and the importance to the consumer of the loan or related supporting property), or to whether the loan is secured by the principal residence of the consumer. In addition, consistent with Dodd-Frank Act section 1405(b), for the reasons discussed above, the Bureau believes that exempting nonprofit small servicers from the requirements of TILA section 128(f) would be in the interest of consumers and in the public interest.

As noted above, current Regulation X cross-references the definition of small servicer in § 1026.41(e)(4) for the purpose of exempting small servicers from several mortgage servicing requirements. Accordingly, in proposing to amend that definition, the Bureau is also proposing to amend the current Regulation X exemptions for small servicers. For this purpose, the Bureau is relying on the same authorities on which it relied in promulgating the current Regulation X small servicer exemptions. Specifically, the Bureau is proposing to exempt nonprofit small servicers from the requirements of Regulation X §§ 1024.38 through 41, except as otherwise provided in § 1024.41(j), *see* § 1024.30(b)(1), as well as certain requirements of § 1024.17(k)(5), pursuant to its authority under section 19(a) of RESPA to grant such reasonable exemptions for classes of transactions as may be necessary to achieve the consumer protection purposes of RESPA. The consumer protection purposes of RESPA include helping borrowers avoid unwarranted or unnecessary costs and fees. The Bureau believes that the proposed rule would ensure consumers avoid unwarranted and unnecessary costs and fees by encouraging nonprofit small servicers to consolidate servicing functions.

In addition, the Bureau relies on its authority pursuant to section 1022(b) of the Dodd-Frank Act to prescribe regulations necessary or appropriate to carry out the purposes and objectives of Federal consumer financial law, including the purposes and objectives of Title X of the Dodd-Frank Act. Specifically, the Bureau believes that the proposed rule is necessary and appropriate to carry out the purpose under section 1021(a) of the Dodd-Frank Act of ensuring that all consumers have access to markets for consumer financial products and services that are fair, transparent, and competitive, and the objective under section 1021(b) of the Dodd-Frank Act of ensuring that markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation.

With respect to §§ 1024.17(k)(5), 39, and 41 (except as otherwise provided in § 1024.41(j)), the Bureau is also proposing the nonprofit small servicer definition pursuant to its authority in section 6(j)(3) of RESPA to set forth requirements necessary to carry out section 6 of

RESPA and in section 6(k)(1)(E) of RESPA to set forth obligations appropriate to carry out the consumer protection purposes of RESPA.

Section 1026.43 Minimum Standards for Transactions Secured by a Dwelling

43(a) Scope

43(a)(3)

The Bureau is proposing to amend the nonprofit small creditor exemption from the ability-to-repay rule that is set forth in § 1026.43(a)(3)(v)(D) of Regulation Z. To qualify for this exemption, a creditor must have extended credit secured by a dwelling no more than 200 times during the calendar year preceding receipt of the consumer's application. The proposal would exclude certain subordinate-lien transactions from this credit extension limit.

Section 129C(a)(1) of TILA states that no creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination (based on verified and documented information) that, at the time the loan is consummated, the consumer has a reasonable ability to repay the loan, according to its terms, and all applicable taxes, insurance (including mortgage guarantee insurance), and assessments. 15 U.S.C. 1639c(a)(1). Section 1026.43 of Regulation Z implements the ability-to-repay provisions of section 129C of TILA.

The January 2013 ATR Final Rule implemented statutory exemptions from the ability-to-repay provisions for home equity lines of credit subject to 12 CFR 1026.40, and for mortgage transactions secured by a consumer's interest in a timeshare plan, as defined in 11 U.S.C. 101(53D). *See* 12 CFR 1026.43(a). The rule also exempted from the ability-to-repay requirements (1) a transaction that is a reverse mortgage subject to 12 CFR 1026.33, (2) temporary or "bridge" loans with a term of 12 months or less, and (3) a construction phase of 12 months or less of a construction-to-permanent loan.

The January 2013 ATR Final Rule did not provide additional exemptions sought by certain commenters in response to an earlier proposal published by the Board in 2011. *See* 76 FR 27389 (May 11, 2011) (2011 ATR Proposal). However, the January 2013 ATR Proposal sought additional input on some of those exemptions, and contained a specific proposal to exempt certain nonprofit creditors from the ability-to-repay requirements. The Bureau believed that limiting the proposed exemption to creditors designated as nonprofits was appropriate because of the difference in lending practices between nonprofit and other creditors. The proposed exemption was premised on the belief that the additional costs imposed by the ability-to-repay requirements might prompt some nonprofit creditors to cease extending credit, or substantially limit their credit activities, thereby possibly harming low- to moderate-income consumers. The Bureau further stated that for-profit creditors derive more revenue from mortgage lending activity than nonprofit creditors, and therefore presumably are more likely to have the resources to comply with the ability-to-repay requirements.

The Bureau was concerned that an exemption for *all* nonprofit creditors could allow irresponsible creditors to intentionally circumvent the ability-to-repay requirements and harm consumers. Thus, under the January 2013 ATR Proposal, the exemption would have been available only if the creditor and the loan met certain criteria. First, the creditor would have been required to have a tax exemption ruling or determination letter from the Internal Revenue Service under section 501(c)(3) of the Internal Revenue Code of 1986 to be eligible for the proposed exemption. Second, the creditor could not have extended credit secured by a dwelling more than 100 times in the calendar year preceding receipt of the consumer's application. Third, the creditor, in the calendar year preceding receipt of the consumer's application, must have extended credit only to consumers whose income did not exceed the low- and moderate-income household limit established by HUD. Fourth, the extension of credit must have been to a consumer with income that does not exceed HUD's low- and moderate-income household limit. Fifth, the creditor must have determined, in accordance with written procedures, that the consumer has a reasonable ability to repay the extension of credit.

The Bureau believed that, in contrast to for-profit creditors and other nonprofit creditors, the nonprofit creditors identified in § 1026.43(a)(3)(v)(D) appeared to elevate long-term community stability over the creditor's economic considerations and to have stronger incentives to determine whether a consumer has the ability to repay a mortgage loan. The Bureau solicited comment regarding whether the proposed exemption was appropriate. The Bureau also specifically requested feedback on whether the proposed credit extension limit of 100 transactions was appropriate or should be increased or decreased. The Bureau also requested comment on the costs that would be incurred by nonprofit creditors that exceed that limit; the extent to which these additional costs would affect the ability of nonprofit creditors to extend responsible, affordable credit to low- and moderate-income consumers; and whether consumers could be harmed by the proposed exemption.

Comments Concerning the 100-Credit Extension Limit

The Bureau received many comments regarding the proposed nonprofit exemption. *See* 78 FR 35429, 35466-67 (June 12, 2013). Most commenters who supported the proposed exemption urged the Bureau to adopt conditions to prevent creditors from using the exemption to circumvent the rule. While many industry representatives, consumer advocates, and nonprofits believed that a 100-credit extension limit would discourage sham nonprofit creditors from exploiting the exemption, several of these commenters asked the Bureau to raise the limit. The commenters were primarily concerned that, in response to the proposed limit, nonprofit creditors would limit certain types of lending. Specifically, a few commenters stated that nonprofit creditors that offer both home-purchase mortgage loans and small-dollar mortgage loans, such as for home energy improvement, would limit small-dollar lending to remain under the 100-credit extension limitation.

The Nonprofit Exemption as Adopted

The May 2013 ATR Final Rule finalized the nonprofit exemption substantially as proposed, but raised the credit extension limit from 100 to 200 credit extensions in the calendar year preceding receipt of the consumer's application. *See* 78 FR 35429, 35467-69 (June 12, 2013). In finalizing the exemption, the Bureau noted that most commenters believed a credit extension limitation was necessary to prevent unscrupulous creditors from exploiting the exemption. The Bureau concluded that the risks of evasion warranted adopting the limit. The Bureau was concerned, however, that the proposed 100-credit extension limit would effectively restrict nonprofits to 50 home-purchase transactions per year, because nonprofits frequently provide simultaneous primary- and subordinate-lien financing for such transactions. Also, the Bureau was concerned that the proposed limit would reduce certain types of small-dollar lending by nonprofits, including financing home energy improvements.

Accordingly, the Bureau included a 200-credit extension limit in the final rule to address the concerns raised by commenters regarding access to credit. Some commenters had suggested limits as high as 500 credit extensions per year; however, the Bureau believed that creditors originating more than 200 dwelling-secured credit extensions per year generally have the resources to bear the implementation and compliance burden associated with the ability-to-repay requirements, such that they can continue to lend without negative impacts on consumers. The final rule did not distinguish between first- and subordinate-liens for purposes of the exemption, as some commenters suggested. The Bureau believed that such a distinction would be needlessly restrictive and it would be more efficient to allow nonprofit creditors to determine the most efficient allocation of funds between primary- and subordinate-lien financing.

Response to the May 2013 ATR Final Rule and Further Proposal

Since the adoption of the May 2013 ATR Final Rule, the Bureau has heard concerns from some nonprofit creditors about the treatment of certain subordinate-lien programs under the nonprofit exemption from the ability-to-repay requirements. These creditors are concerned that they may be forced to curtail these subordinate-lien programs or more generally limit their lending activities to avoid exceeding the 200-credit extension limit. In particular, these entities have indicated concern with the treatment of subordinate-lien transactions that charge no interest and for which repayment is generally either forgivable or of a contingent nature. The Bureau understands that, absent an amended nonprofit exemption from the May 2013 ATR Final Rule, these nonprofit creditors may not have the resources to comply with the rule and therefore are likely to curtail their lending to stay within the 200-credit extension limit.

In light of these concerns, the Bureau is proposing to exclude certain deferred or contingent, interest-free subordinate liens from the 200-credit extension limit for purposes of the nonprofit exemption in § 1026.43(a)(3)(v)(D). Specifically, proposed § 1026.43(a)(3)(vii) would provide that consumer credit transactions that meet the following criteria are not considered in determining whether a creditor meets the requirements of § 1026.43(a)(3)(v)(D)(*1*): (A) the transaction is secured by a subordinate lien; (B) the transaction is for the purpose of downpayment, closing costs, or other similar home buyer assistance, such as principal or interest subsidies, property rehabilitation assistance, energy efficiency assistance, or foreclosure avoidance or prevention; (C) the credit contract does not require payment of interest; (D) the credit contract provides that the repayment of the amount of credit extended is (*1*) forgiven incrementally or in whole, at a date certain, and subject only to specified ownership and occupancy conditions, such as a requirement that the consumer maintain the property as the consumer's principal dwelling for five years, (*2*) deferred for a minimum of 20 years after consummation of the transaction, (*3*) deferred until sale of the property securing the transaction, or (*4*) deferred until the property securing the transaction is no longer the principal dwelling of the consumer; (E) the total of costs payable by the consumer in connection with the transaction at consummation is less than 1 percent of the amount of credit extended and includes no charges other than fees for recordation of security instruments, deeds, and similar documents; a bona fide and reasonable application fee; and a bona fide and reasonable fee for housing counseling services; and (F) in connection with the transaction, the creditor complies with all other applicable requirements of Regulation Z.

Proposed comment 43(a)(3)(vii)-1 would provide that the terms of the credit contract must satisfy the conditions that the transaction not require the payment of interest under § 1026.43(a)(3)(vii)(C) and that repayment of the amount of credit extended be forgiven or deferred in accordance with § 1026.43(a)(3)(vii)(D). The comment would further provide that the other requirements of § 1026.43(a)(3)(vii) need not be reflected in the credit contract, but the creditor must retain evidence of compliance with those provisions, as required by the record retention provisions of § 1026.25(a). In particular, the creditor must have information reflecting that the total of closing costs imposed in connection with the transaction are less than 1 percent of the amount of credit extended—and include no charges other than recordation, application, and housing counseling fees, in accordance with § 1026.43(a)(3)(vii)(E). Unless an itemization of the amount financed sufficiently details this requirement, the creditor must establish compliance with § 1026.43(a)(3)(vii)(E) by some other written document and retain it in accordance with § 1026.25(a).

Proposed § 1026.43(a)(3)(vii) and the accompanying comment largely mirror a provision that was finalized as part of the Bureau's December 2013 TILA-RESPA Final Rule. *See* 78 FR 79729 (Dec. 31, 2013). That provision, which was finalized in both Regulation X, at § 1024.5(d), and Regulation Z, at § 1026.3(h)—and which will take effect on August 1, 2015, provides a partial exemption from the integrated disclosure requirements for loans that meet the above-described criteria. The Bureau finalized this partial exemption in the December 2013 TILA-RESPA Final Rule to preserve an existing exemption from Regulation X issued by HUD and to facilitate compliance with TILA and RESPA. *See* 78 FR 79729, 79758 and 79772 (Dec. 31, 2013). In proposing that exemption, the Bureau explained that the exemption was intended to describe criteria associated with certain housing assistance loan programs for low- and moderate-income persons. *See* 77 FR 51115, 51138 (Aug. 23, 2012). The Bureau believes the same criteria describe the class of transactions that may appropriately be excluded from the 200-credit extension limit in the ability-to-repay exemption for nonprofits. The Bureau also believes that defining a single class of transactions for purposes of § 1024.5(d), § 1026.3(h), and § 1026.43(a)(3)(vii) may facilitate compliance for creditors.

The Bureau believes the § 1026.43(a)(3)(v)(D) exemption as amended by the proposal would be limited to creditors with characteristics that ensure consumers are offered responsible, affordable credit on reasonably repayable terms. The Bureau also believes that subordinate-lien transactions meeting the proposed exclusion's criteria pose low risk to consumers, and that excluding these transactions from the credit extension limit is consistent with TILA's purposes. For example, in transactions that would be covered by proposed § 1026.43(a)(3)(vii), consumers often benefit from a reduction in their repayment obligations on an accompanying first-lien mortgage and often control the triggering of any subordinate-lien repayment requirement for at least a twenty-year period. Therefore, the subordinate-lien transactions may enhance the consumer's ability to repay their monthly mortgage obligations. Further, the prohibition against charging interest and strict limitation on fees reduces the likelihood that borrowers will be misled about the extent of their financial obligations, as the amounts of their obligations (if at all repayable) remain essentially fixed. The Bureau believes that limiting the exclusion to loans with these characteristics may also reduce the likelihood that the provision would be used to evade the ability-to-repay requirements.

The Bureau also believes the proposed exclusion would facilitate access to credit for low- and moderate-income consumers. As noted above, the proposed exclusion would apply to subordinate-lien financing extended only for specified purposes, including home buyer assistance, property rehabilitation, or foreclosure avoidance. The Bureau believes that such financing plays a critical role in nonprofit lending to low- and moderate-income consumers, and in particular homeownership programs designed for such consumers. In purchase-money transactions, subordinate-lien financing may reduce the amortizing payment on first-lien mortgages, improving low- and moderate-income consumers' ability to repay, especially in jurisdictions where housing costs are high. Similarly, the Bureau believes such financing may play a critical role in nonprofit creditors' efforts to provide property-rehabilitation, energy-efficiency, and foreclosure-avoidance assistance.

The Bureau believes that, without the proposed exclusion for these transactions, nonprofit creditors may limit such extensions of credit, or may limit their overall credit activity. As a result, low- and moderate-income consumers who would otherwise qualify for a nonprofit creditor's program may be denied credit. As noted in the January 2013 ATR Proposal, the current exemption for nonprofit creditors was premised on the belief that the additional costs imposed by the ability-to-repay requirements might prompt certain nonprofit creditors to cease extending credit, or substantially limit their credit activities, thereby possibly harming low- and moderate-income consumers. *See* 78 FR 6621, 6645 (Jan. 30, 2013). Because of their limited resources to bear the compliance burden of the ability-to-repay rule, the Bureau believes at least some nonprofit creditors may limit lending activity to maintain their exemption. The proposed amendment to the § 1026.43(a)(3)(v)(D) exemption is intended to minimize this effect by allowing nonprofit creditors to originate subordinate-lien transactions meeting the proposed § 1026.43(a)(3)(vii) criteria without the risk of losing that exemption.

In addition, the Bureau believes that excluding these subordinate-lien transactions from the transaction-count limitation may be appropriate because the origination of these loans is not necessarily indicative of a creditor's capacity to comply with the ability-to-repay requirements. As noted above, the Bureau believes that creditors extending credit in more than 200 dwelling-secured transactions per year are likely to have the resources and capacity to comply with the ability-to-repay requirements. However, subordinate-lien transactions typically involve small loan amounts and, as limited by the proposed exclusion's criteria, would generate little revenue to support a creditor's capacity to comply. Absent the exclusion, those creditors might curtail lending—with potential negative impacts for consumer's access to credit. Particularly when such a subordinate-lien transaction is originated in connection with a first-lien transaction, counting both transactions towards the 200-credit extension limit may not provide the appropriate indication of a creditor's capacity to comply.

As noted above, in adopting the current nonprofit exemption in § 1026.43(a)(3)(v)(D), the Bureau did not distinguish between first- and subordinate-lien transactions for purposes of the credit extension limit out of concerns that doing so would affect creditors' allocations of loans. However, the Bureau does not believe the proposed exclusion is likely to significantly affect such allocations. As noted above, the proposed exclusion permits nonprofit creditors to allocate resources to subordinate-lien transactions without risking their exemption from the ability-to-repay rule. To the extent the proposed exclusion encourages origination of these subordinate-lien transactions, the Bureau believes that the limitations on the borrower's repayment obligations as well as on the creditor's ability to charge interest and fees may minimize the risk that, as a result of the exclusion, creditors would allocate greater amounts of their lending to these transactions. In fact, to the extent many affordable homeownership programs use such subordinate-lien transactions in tandem with first-lien mortgages, excluding these subordinate-lien transactions from the credit extension limit count may reduce the current § 1026.43(a)(3)(v)(D) exemption's impact on nonprofit creditors' allocation of financing between first- and subordinate-lien transactions.

To address nonprofit creditor concerns, the Bureau also considered whether it would be appropriate to remove the credit extension limitation from the § 1026.43(a)(3)(v)(D) nonprofit exemption altogether. The Bureau believes that nonprofit creditors who originate 200 or more dwelling-secured transactions in a year generally have the resources necessary to comply with TILA ability-to-repay requirements. The Bureau believes that the exemption properly balances relevant considerations, including the nature of credit extended, safeguards and other factors that may protect consumers from harm, and the extent to which application of the regulatory requirements would affect access to responsible, affordable credit. Accordingly, the Bureau continues to believe that the credit extension limit is necessary to prevent evasion, but is proposing to exclude from the 200-credit extension limit a narrow class of subordinate-lien transactions to address concerns expressed by nonprofit creditors and avoid potential negative impacts on access to credit, particularly for low- and moderate-income consumers.

Legal Authority

The current § 1026.43(a)(3)(v)(D) exemption from the ability-to-repay requirements was adopted pursuant to the Bureau's authority under section 105(a) and (f) of TILA. Pursuant to section 105(a) of TILA, the Bureau generally may prescribe regulations that provide for such adjustments and exceptions for all or any class of transactions that the Bureau judges are necessary or proper to effectuate, among other things, the purposes of TILA. For the reasons discussed in more detail above, the Bureau believes that the proposed amendment of the current § 1026.43(a)(3)(v)(D) exemption from the TILA ability-to-repay requirements is necessary and proper to effectuate the purposes of TILA, which include the purposes of TILA section 129C. The Bureau believes that the proposed amendment of the exemption ensures that consumers are offered and receive residential mortgage loans on terms that reasonably reflect their ability to repay by helping to ensure the viability of the mortgage market for low- and moderate-income consumers. The Bureau believes that the mortgage loans originated by nonprofit creditors identified in § 1026.43(e)(4)(v)(D) generally account for a consumer's ability to repay. Without the proposed amendment to the exemption, the Bureau believes that low- and moderate-income consumers might be at risk of being denied access to the responsible and affordable credit offered by these creditors, which is contrary to the purposes of TILA. The proposed amendment to the exemption is consistent with the purposes of TILA by ensuring that consumers are able to obtain responsible, affordable credit from the nonprofit creditors discussed above.

The Bureau has considered the factors in TILA section 105(f) and believes that, for the reasons discussed above, the proposed amendment of the exemption is appropriate under that provision. For the reasons discussed above, the Bureau believes that the proposed amendment to § 1026.43(a)(3)(v)(D) would exempt extensions of credit for which coverage under the ability-to-repay requirements does not provide a meaningful benefit to consumers (in the form of useful information or protection) in light of the protection that the Bureau believes the credit extended by these creditors already provides to consumers. The Bureau believes that the proposed amendment to the § 1026.43(a)(3)(v)(D) exemption is appropriate for all affected consumers, regardless of their other financial arrangements and financial sophistication and the importance of the loan and supporting property to them. Similarly, the Bureau believes that the proposed amendment to the § 1026.43(a)(3)(v)(D) exemption is appropriate for all affected loans covered under the exemption, regardless of the amount of the loan and whether the loan is secured by the principal residence of the consumer. Furthermore, the Bureau believes that, on balance, the proposed amendment to the § 1026.43(a)(3)(v)(D) exemption will simplify the credit process without undermining the goal of consumer protection, denying important benefits to consumers, or increasing the expense of (or otherwise hindering) the credit process.

43(e) Qualified Mortgages

43(e)(3) Limits on Points and Fees for Qualified Mortgages

The Dodd-Frank Act provides that “qualified mortgages” are entitled to a presumption that the creditor making the loan satisfied the ability-to-repay requirements. The qualified mortgage provisions are implemented in § 1026.43(e). Current § 1026.43(e)(3)(i) provides that a covered transaction is not a qualified mortgage if the transaction’s total points and fees exceed certain limits set forth in § 1026.43(e)(3)(i)(A) through (E). For the reasons set forth below, the

Bureau is proposing to permit a creditor or assignee to cure an inadvertent excess over the qualified mortgage points and fees limits by refunding to the consumer the amount of excess, under certain conditions. As discussed in part VI.A. below, the Bureau is also requesting comment on issues related to inadvertent debt-to-income ratio overages, but at this time is not proposing a specific change to the regulation. For purposes of these discussions, "cure" means a procedure to reduce points and fees or debt-to-income ratios after consummation when the qualified mortgage limits have been inadvertently exceeded, while "correction" means post-consummation revisions to documentation or calculations, or both, to reflect conditions as they actually existed at consummation.

43(e)(3)(i)

As discussed below, the Bureau is proposing a new § 1026.43(e)(3)(iii) to establish a cure procedure where a creditor inadvertently exceeds the qualified mortgage points and fees limits, under certain conditions. As a conforming change, the Bureau is also proposing to amend § 1026.43(e)(3)(i), to add the introductory phrase "Except as provided in paragraph (e)(3)(iii) of this section" to § 1026.43(e)(3)(i), to specify that the cure provision in proposed § 1026.43(e)(3)(iii) is an exception to the general rule that a covered transaction is not a qualified mortgage if the transaction's total points and fees exceed the applicable limit set forth in § 1026.43(e)(3)(i)(A) through (E).

43(e)(3)(iii)

Section 1411 of the Dodd-Frank Act added new TILA section 129C to require a creditor making a residential mortgage loan to make a reasonable and good faith determination (based on verified and documented information) that, at the time the loan is consummated, the consumer has a reasonable ability to repay the loan. 15 U.S.C. 1639c. TILA section 129C(b) further provides that the ability-to-repay requirements are presumed to be met if the loan is a qualified mortgage. TILA section 129C(b)(2) sets certain product-feature and underwriting requirements for qualified mortgages, including a 3-percent limit on points and fees, but gives the Bureau authority to revise, add to, or subtract from these requirements.[15] Those requirements are implemented by the January 2013 ATR Final Rule, as amended by the May 2013 ATR Final Rule.

The current ability-to-repay rule provides for four categories of qualified mortgages: a "general" qualified mortgage definition that is available to any creditor;[16] a temporary qualified mortgage definition for loans eligible for sale to or guarantee by a government sponsored enterprise (GSE) or eligible for guarantee by or insurance under certain Federal agency programs;[17] and two qualified mortgage definitions available to small creditors.[18] The current rule provides that for all types of qualified mortgages, the up-front points and fees charged in connection with the mortgage must not exceed 3 percent of the total loan amount, with higher thresholds specified for various categories of loans below $100,000.[19] Pursuant to

[15] *See* TILA section 129C(b)(3)(B)(i). TILA section 129C(b)(2)(D) requires the Bureau to prescribe rules adjusting the 3-percent points and fees limit to "permit lenders that extend smaller loans to meet the requirements of the presumption of compliance."

[16] 12 CFR 1026.43(e)(2). Under the general qualified mortgage definition, the loan must meet certain restrictions on loan features, points and fees, and underwriting.

[17] Section 1026.43(e)(4). The temporary GSE/agency qualified mortgage definition will sunset on the earlier of January 10, 2021, or, with respect to GSE-eligible loans, when the GSEs exit government conservatorship, or, with respect to agency-eligible loans, when those agencies' qualified mortgage definitions take effect.

[18] Section 1026.43(e)(5) contains a special qualified mortgage definition for small creditors that hold loans in portfolio, while § 1026.43(f) permits small creditors that operate predominantly in rural or underserved areas to originate qualified mortgages with balloon-payment features, despite the general prohibition on qualified mortgages containing balloon payments. For a two-year transitional period, § 1026.43(e)(6) permits all small creditors, regardless of their areas of operation, to originate qualified mortgages with balloon-payment features. "Small creditor" is defined in § 1026.35(b)(2)(iii)(B) and (C), and generally includes creditors that, in the preceding calendar year, originated 500 or fewer covered transactions, including transactions originated by affiliates, and had less than $2 billion in assets.

[19] *See* § 1026.43(e)(2) and (3). For loans of $60,000 up to $100,000, § 1026.43(e)(3)(i) allows points and fees of no more than $3,000. For loans of $20,000 up to $60,000, § 1026.43(e)(3)(i) allows points and fees of no more than 5 percent of the total loan amount. For loans of $12,500 up to $20,000, § 1026.43(e)(3)(i) allows points and fees of no more than $1,000. For loan amounts less than $12,500, § 1026.43(e)(3)(i) allows points and fees of no more than 8 percent of the total loan amount.

§ 1026.32(b)(1), points and fees are the "fees or charges that are known at or before consummation."

The calculation of points and fees is complex and can involve the exercise of judgment that may lead to inadvertent errors with respect to charges imposed at or before consummation. For example, discount points may be mistakenly excluded from, or included in, the points and fees calculation as bona fide third-party charges, or bona fide discount points, under § 1026.32(b)(1)(i)(D) or (E). Mortgage insurance premiums under § 1026.32(b)(1)(i)(C) or loan originator compensation under § 1026.32(b)(1)(ii) may also mistakenly be excluded from, or included in, the points and fees calculation. A rigorous post-consummation review by the creditor or assignee of loans originated with the good faith expectation of qualified mortgage status may uncover such inadvertent errors. However, the current rule does not provide a mechanism for curing such inadvertent points and fees overages that are discovered after consummation.

Based on information received in the course of outreach in connection with the Bureau's Implementation Plan, the Bureau understands that some creditors may not originate, and some secondary market participants may not purchase, mortgage loans that are near the qualified mortgage limits on points and fees because of concern that the limits may be inadvertently exceeded at the time of consummation. Specifically, the Bureau understands that some creditors seeking to originate qualified mortgages may establish buffers, set at a level below the points and fees limits in § 1026.43(e)(3)(i), to avoid exceeding those limits. Those creditors may simply refuse to extend mortgage credit to consumers whose loans would exceed the buffer threshold, either due to the creditors' concerns about the potential liability attending loans originated under the general ability-to-repay standard or the risk of repurchase demands from the secondary market if the qualified mortgage points and fees limit is later found to have been exceeded. Where such buffers are established, the Bureau is concerned that access to credit for consumers seeking loans at the margins of the limits might be negatively affected. The Bureau is also concerned that creditors may increase the cost of credit for consumers seeking loans at the margins of the limits due to compliance or secondary market repurchase risk.

In light of these concerns, the Bureau is proposing to permit a creditor or assignee to cure an inadvertent excess over the qualified mortgage points and fees limit under certain defined conditions, including the requirement that the loan was originated in good faith as a qualified mortgage and that the cure be provided in the form of a refund to the consumer within 120 days after consummation. The Bureau notes that, where the loan was originated in good faith as a qualified mortgage, consumers likely received the benefit of qualified mortgage treatment by receiving lower overall loan pricing. For this reason, the Bureau believes that a cure provision, if appropriately limited, would reflect the expectations of both consumers and creditors at the time of consummation, would not result in significant consumer harm, and may increase access to credit by encouraging creditors to extend credit to consumers seeking loans at the margins of the points and fees limits. In addition, the Bureau believes that a limited cure provision may promote consistent pricing within the qualified mortgage range by decreasing the market's perceived need for higher pricing (due to compliance or secondary market repurchase risk) at the margins of the points and fees limits. The Bureau also believes this would promote stability in the market by limiting the need for repurchase demands that may otherwise be triggered without the proposed cure option.

The Bureau expects that, over time, creditors will develop greater familiarity with, and capabilities for, originating loans that are not qualified mortgages under the general ability-to-repay requirements, as well as greater confidence in general compliance systems. As they do so, creditors may relax internal buffers regarding points and fees that are predicated on the qualified mortgage threshold. However, the Bureau believes the impacts on access to credit may make a points and fees cure provision appropriate at this time. In addition, the Bureau believes that the cure provision will encourage post-consummation quality control review of loans, which will improve the origination process over time.

Accordingly, proposed § 1026.43(e)(3)(iii) would provide that if the creditor or assignee determines after consummation that the total points and fees payable in connection with a loan exceed the applicable limit under § 1026.43(e)(3)(i), the loan is not precluded from being a qualified mortgage if certain conditions, discussed below, are met.

43(e)(3)(iii)(A)

First, new § 1026.43(e)(3)(iii)(A) would require that the creditor originated the loan in good faith as a qualified mortgage and the loan otherwise meets the requirements of § 1026.43(e)(2), (e)(4), (e)(5), (e)(6), or (f), as applicable. Comment 43(e)(3)(iii)-1 would provide examples of circumstances that may be evidence that a loan was or was not originated in good faith as a qualified mortgage. First, the comment would provide that maintaining and following policies and procedures designed to ensure that points and fees are correctly calculated and do not exceed the applicable limit under § 1026.43(e)(3)(i) may be evidence that the creditor originated the loan in good faith as a qualified mortgage. In addition, the comment would provide that if the pricing on the loan is consistent with pricing on qualified mortgages originated contemporaneously by the same creditor, that may be evidence that the loan was originated in good faith as a qualified mortgage. The comment would also provide examples of circumstances that may be evidence that the loan was not originated in good faith as a qualified mortgage.

Specifically, the comment would provide that, if a creditor does not maintain—or has but does not follow—policies and procedures designed to ensure that points and fees are correctly calculated and do not exceed the applicable limit described in § 1026.43(e)(3)(i), that may be evidence that the creditor did not originate the loan in good faith as a qualified mortgage. If the pricing on the loan is not consistent with pricing on qualified mortgages originated contemporaneously by the same creditor, that may also be evidence that a loan was not originated in good faith as a qualified mortgage.

The Bureau is proposing to allow for a post-consummation cure of points and fees overages only where the loan was originated in good faith as a qualified mortgage to ensure that the cure provision is available only to creditors who make inadvertent errors in the origination process and to prevent creditors from exploiting the cure provision by intentionally exceeding the points and fees limits. However, the Bureau seeks comment on whether the good faith element of § 1026.43(e)(3)(iii)(A) is necessary in light of the other proposed limitations on the cure provision. The Bureau also seeks comment on the proposed examples in comment 43(e)(3)(iii)-1, specifically including whether additional guidance regarding the term "contemporaneously" in comments 43(e)(3)-1.i.B and 43(e)(3)-1.ii.B is necessary, and whether additional examples would be useful.

43(e)(3)(iii)(B)

Second, to cure a points and fees overage, proposed § 1026.43(e)(3)(iii)(B) would require that within 120 days after consummation, the creditor or assignee refunds to the consumer the dollar amount by which the transaction's points and fees exceeded the applicable limit under § 1026.43(e)(3)(i) at consummation.

The Bureau believes that requiring a refund to occur within a short period after consummation is consistent with the requirement that the loan be originated in good faith as a qualified mortgage. The Bureau understands that many creditors and secondary market purchasers conduct audits or quality control reviews of loan files in the period immediately following consummation to ensure, among other things, compliance with regulatory requirements. During this review phase, a creditor that originated a loan in good faith as a qualified mortgage (or the creditor's assignee) may discover an inadvertent points and fees overage. Indeed, providing a reasonable but limited time period for cure may actually promote strong post-consummation quality control efforts, which may, in turn, improve a creditor's origination procedures and compliance, thereby reducing the use of the cure mechanism over time. Strong post-consummation quality control and improved origination procedures may also reduce costs over time and decrease the incidence of repurchase demands after a loan is sold into the secondary market.

The Bureau believes that the proposed 120-day period would result in reasonably prompt refunds to affected consumers and provide sufficient time to accommodate communication with the consumer. A 120-day period should also allow sufficient time for creditors and secondary market participants to conduct post-consummation reviews that may uncover inadvertent points and fees overages. In contrast, a longer period would not result in prompt refunds and would provide less incentive for rigorous review immediately after consummation. In outreach to industry stakeholders prior to this proposal, the Bureau learned that 120 days is a time period within which post-consummation quality control reviews generally are completed. The Bureau specifically requests comment more broadly, however, on whether 120 days is an appropriate time period for post-consummation cure of a points and fees overage, or whether a longer or shorter period should be provided; what factors would support any recommended time period; and, if the cure were available for a longer period, whether additional conditions should be applied beyond those in this proposal.

The Bureau considered whether the cure provision should run from the date of discovery of the points and fees overage or within a limited number of days after transfer of the loan, rather than the time of consummation, but the Bureau believes that such alternative provisions would be inappropriate. The Bureau is concerned that allowing an extended period of time for cure would create incentives for bad faith actors to intentionally violate the points and fees limit and selectively wait for discovery to cure the violation only when it would be to their advantage to do so. Such actions would not be consistent with the statutory requirement of making a good faith determination of a consumer's ability-to-repay. Similarly, the Bureau is concerned that, particularly later in the life of the loan, giving the creditor a unilateral option to change the status of the loan to a qualified mortgage, thereby providing the creditor with enhanced protection from liability, would facilitate evasion of regulatory requirements by the creditor.

The Bureau also considered whether it would be appropriate to limit a creditor's or assignee's ability to cure points and fees overages for qualified mortgage purposes to the time prior to the receipt of written notice of the error from or the institution of any action by the consumer. The Bureau believes that such a requirement may not be necessary because the points and fees cure must occur within 120 days after consummation such that it is unlikely that the consumer would provide such notice or institute such action during that period. Further, the Bureau believes that such a requirement might undercut the purposes of the cure provision—to encourage both lending up to the points and fees limits and post-consummation quality control review of loans—since creditors and assignees could not be certain of their ability to review the loan post-consummation and provide a refund, if appropriate. However, the Bureau solicits comment on whether cure should be permitted only prior to receipt of written notice of the error from or the institution of any action by the consumer.

The Bureau recognizes that, where points and fees have been financed as part of the loan amount and an overage is refunded to the consumer after consummation, the consumer will continue to pay interest on a loan amount that includes the overage. As a result, the consumer may pay more interest over the life of the loan than would have been paid absent the inadvertent points and fees overage. Although the Bureau believes such circumstances will be limited, the Bureau acknowledges that a post-consummation refund of the amount of points and fees overage alone would not make the consumer whole in most such cases.[20] For this reason, the Bureau considered whether the cure provision should require other means of restitution to the consumer, such as restructuring the loan to provide a lower loan amount commensurate with deducting the points and fees overage, or requiring any refund to the consumer to include the present value of excess interest that the consumer would pay over the life of the loan. However, the Bureau believes there are complications to these approaches. For example, the Bureau expects that creditors would have difficulty systematically restructuring loans within a short time after consummation, especially where the loan has already been, or shortly will be, securitized. The Bureau also notes potential difficulties in determining the period over which excess interest should be calculated, since few consumers hold their loans for the entire loan term. In light of these considerations, the Bureau is not proposing that the cure provision require any means of restitution other than a refund of the actual overage amount to the consumer. However, the

[20] There may be circumstances where the consumer pays discount points to obtain a lower interest rate and the post-consummation review determines the payments do not qualify as bona fide discount points. In such cases, a refund of the discount points, without additional changes to the loan, may result in a net benefit to the consumer.

Bureau solicits comment on other appropriate means of restitution and in what circumstances they may be appropriate.

43(e)(3)(iii)(C)

The third criteria for a cure is set forth in proposed § 1026.43(e)(3)(iii)(C), which would provide that the creditor or assignee must maintain and follow policies and procedures for post-consummation review of loans and for refunding to consumers amounts that exceed the applicable limit under § 1026.43(e)(3)(i). Comment 43(e)(3)(iii)-2 would provide that a creditor or assignee satisfies § 1026.43(e)(3)(iii) if it maintains and follows policies and procedures for post-consummation quality control loan review and for curing (by providing a refund) errors in points and fees calculations that occur at or before consummation.

The Bureau believes this requirement will provide an incentive for creditors to maintain rigorous quality control measures on a consistent and continuing basis. The Bureau believes that conditioning a cure on a consistently applied policy promotes and incentivizes good faith efforts to identify and minimize errors that may occur at or before consummation, with resulting benefits to consumers, as well as creditors and assignees.

The Bureau requests comment on all aspects of the proposal to permit creditors to cure inadvertent excesses over the points and fees limit, including whether a post-consummation cure should be permitted, and whether different, additional, or fewer conditions should be imposed upon its availability, such as whether the consumer must be current on loan payments at the time of the cure.

Legal Authority

The Bureau proposes § 1026.43(e)(3)(iii) pursuant to its authority under TILA section 129C(b)(3)(B)(i) to promulgate regulations that revise, add to, or subtract from the criteria that define a qualified mortgage. For the reasons discussed above, the Bureau believes that the proposed provision is warranted under TILA section 129C(b)(3)(B)(i) because the proposal is necessary and proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with purposes of section 129C of TILA, and also necessary and appropriate to facilitate compliance with section 129C of TILA. For example, the Bureau believes the proposed limited post-consummation cure provision will facilitate compliance with TILA section 129C by encouraging strict, post-consummation quality control loan reviews that will, over time, improve the origination process.

In addition, because proposed § 1026.43(e)(3)(iii) permits creditors to cure inadvertent non-compliance with the general qualified mortgage points and fees limitation up to 120 days after consummation, the Bureau also proposes § 1026.43(e)(3)(iii) pursuant to its authority under section 105(a) and (f) of TILA. Pursuant to section 105(a) of TILA, the Bureau generally may prescribe regulations that provide for such adjustments and exceptions for all or any class of transactions that the Bureau judges are necessary or proper to, among other things, effectuate the purposes of TILA. For the reasons discussed above, the Bureau believes that exempting the class of qualified mortgages that involve a post-consummation points and fees cure from the statutory requirement that the creditor make a good faith determination that the consumer has the ability to repay "at the time the loan is consummated" is necessary and proper to effectuate the purposes of TILA. The Bureau believes that limited post-consummation cure of points and fees overages will preserve access to credit to the extent it encourages creditors to extend credit to consumers seeking loans with points and fees up to the 3-percent limit. Without a points and fees cure provision, the Bureau believes that some consumers might be at risk of being denied access to responsible, affordable credit, which is contrary to the purposes of TILA. The Bureau also believes a limited post-consummation cure provision will facilitate compliance with TILA section 129C by encouraging strict, post-consummation quality control loan reviews that will, over time, improve the origination process.

The Bureau has considered the factors in TILA section 105(f) and believes that a limited points and fees cure provision is appropriate under that provision. The Bureau believes that the exemption, with the specific conditions required by the proposal, is appropriate for all affected consumers; specifically, those seeking loans at the margins of the points and fees limit whose access to credit may be affected adversely without the exemption. Similarly, the Bureau believes that the exemption is appropriate for all affected loans covered under the exemption, *i.e.* those made in good faith as qualified mortgages, regardless of the amount of the loan and whether the loan is secured by the principal residence of the consumer. Furthermore, the Bureau believes that, on balance, the exemption would not undermine the goal of consumer protection or increase the complexity or expense of (or otherwise hinder) the credit process, because costs may actually decrease, as noted above. While the exemption may result in consumers in affected transactions losing some of TILA's benefits, potentially including some aspects of a foreclosure legal defense, the Bureau believes such potential losses are outweighed by the potentially increased access to responsible, affordable credit, an important benefit to consumers. The Bureau believes that is the case for all affected consumers, regardless of their other financial arrangements, their financial sophistication, and the importance of the loan and supporting property to them.

VI. Other Requests for Comment

A. Request for Comment on Cure or Correction of Debt-to-Income Overages

To satisfy the general qualified mortgage definition in § 1026.43(e)(2), the consumer's total monthly debt-to-income ratio—verified, documented, and calculated in accordance with

§ 1026.43(e)(2)(vi)(B) and appendix Q—cannot exceed 43 percent at the time of consummation.[21] Similar to an error made in calculating points and fees, errors made in calculating debt-to-income ratios could jeopardize a loan's qualified mortgage status under § 1026.43(e)(2). Some industry stakeholders have suggested that creditors seeking to originate § 1026.43(e)(2) qualified mortgages may establish buffers that relate to debt-to-income ratios—*i.e.*, buffers set at a level below the rule's 43-percent debt-to-income ratio limit. Some creditors may, in turn, refuse to extend mortgage credit to consumers whose loans would exceed the buffer threshold, either due to concerns about potential liability associated with loans originated under the general ability-to-repay standard or the risk of repurchase demands from the secondary market, if the debt-to-income ratio limit is exceeded. Such practices may reduce access to credit to consumers at the margins of the debt-to-income ratio limit.

As explained above, the Bureau is proposing § 1026.43(e)(3)(iii) to permit cure of inadvertent points and fees overages by refunding to the consumer the dollar amount that exceeds the applicable points and fees limit, under certain defined conditions. The Bureau is also considering whether a similar cure provision may be appropriate in the context of debt-to-income overages. As discussed above, the proposed points and fees cure procedure may benefit consumers and the market in various ways. A debt-to-income cure provision has the potential to benefit consumers and the market in a similar manner. However, as discussed below, the Bureau believes that miscalculations of debt-to-income ratios are fundamentally different in nature than errors in calculating points and fees, and may be less suitable to a cure provision similar to proposed § 1026.43(e)(3)(iii).

[21] In contrast to the 3-percent cap on points and fees, which applies to all qualified mortgages, the 43-percent debt-to-income ratio limit applies only to the "general" qualified mortgage category (§ 1026.43(e)(2)), and not to the temporary GSE/agency category (§ 1026.43(e)(4)) or the small creditor categories (§ 1026.43(e)(5), (e)(6), and (f)).

The Bureau is also considering whether it may be appropriate to address the more limited scenario where debt-to-income overages result from errors in calculation or documentation, or both, of debt or income. Specifically, the Bureau is considering whether, in such situations, it would be feasible to permit post-consummation corrections to the documentation, which would result in a corresponding recalculation of the debt-to income ratio. While such a correction mechanism has the potential to benefit consumers and the market, there are a number of reasons, discussed below, why it may be inappropriate and impracticable.

In light of these difficulties and concerns, the Bureau is not proposing a specific debt-to-income ratio cure or correction provision at this time. However, to aid its ongoing consideration of these options, the Bureau is requesting comment on any and all aspects of potential cure and correction provisions for debt-to-income overages described below.

Debt-to-Income Cure

As noted, the Bureau recognizes that a debt-to-income cure mechanism has the potential to benefit consumers and the market. However, the Bureau is concerned that such a procedure may be inappropriate because a miscalculation of debt-to-income ratios cannot be remedied in a manner similar to, or as equally practicable as, remedying a miscalculation of points and fees. The Bureau believes that debt-to-income overages commonly would result from creditors incorrectly, but inadvertently, including income or failing to consider debts in accordance with the rule—*i.e.*, understating the numerator or overstating the denominator in the mathematical equation that derives the debt-to-income ratio. In these situations, a creditor or secondary market purchaser would need to alter the consumer's debts and/or income to bring the debt-to-income ratio within the 43-percent limit or the ratio would exceed qualified mortgage limits.

It is unclear how creditors could raise consumers' incomes or lower their debts systematically to bring the ratio within the 43-percent limit. Of course, creditors cannot increase a consumer's income. It may be possible in some situations for creditors to modify the underlying mortgage and lower the consumer's monthly payment on the loan so that the "debt" is low enough to bring the ratio back within the 43-percent limit—or to pay down other debts of the consumer to achieve the same result. However, the Bureau believes this approach would require a complex restructuring of the loan, which may itself trigger a repurchase demand from the secondary market, and possibly require a refund of excess payments collected from the time of consummation.

For any such cure provision to be considered, creditors would need to maintain and follow policies and procedures of post-consummation review of loans to restructure them and refund amounts as necessary to bring the debt-to-income ratio within the 43-percent limit. However, based on the Bureau's current information, the Bureau does not believe creditors could realistically meet such a requirement, and expects that creditors would have difficulty systematically restructuring loans, or systematically paying down debts on the consumer's behalf, within a short time after consummation. Moreover, in some cases the consumer's other debts (when properly considered) could be too substantial, or the corrected income too low, for any viable modification of the mortgage to reduce the debt-to-income ratio below the prescribed limit.

Debt-to-Income Correction

The Bureau is also considering whether it may be appropriate to address the more limited scenario where debt-to-income overages result solely from errors in documentation of debt or income. For example, a creditor may have considered but failed to properly document certain income in accordance with the rule. Such an error may feasibly be remedied by submission of corrected documentation (and a corresponding recalculation of the debt-to-income ratio) without the need for a monetary cure or loan restructuring. A correction also could be effective in situations in which the creditor erred in calculating the consumer's debts and as a result verified and documented only certain income if that income alone appeared sufficient to satisfy the 43-percent limit.

Certain sources of income (*e.g.*, salary) are generally considered easier to document than others (*e.g.*, rental or self-employment income), and satisfaction of the general qualified mortgage definition does not require creditors to document and consider every potential source of income, so long as the debt-to-income ratio based on the income considered (and calculated in accordance with the rule) does not exceed 43 percent. Creditors may, for the sake of expediency, only consider easy-to-document income when that income alone satisfies the debt-to-income ratio—a practice permitted under the regulation.[22] Where a creditor or secondary market purchaser later discovers that income relied upon was overstated or additional debts existed that were not considered, it may be feasible for a creditor to correct a resulting debt-to-income ratio overage by collecting documentation and considering the additional income it knew about at the time of consummation but chose not to consider for the sake of expediency.

While these means of correcting debt-to-income ratio overages may be feasible, the Bureau is concerned that a provision tailored toward these situations may be inappropriate and believes any such provision could result in unintended consequences. The Bureau is concerned about the risk of creating any disincentives for creditors to exercise due diligence in carrying out their statutory obligations. In addition, the Bureau is concerned that allowing creditors to

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[22] *See* comment 43(c)(2)(i)-5; *see also* Appendix Q (noting that a creditor may always "exclude the income or include the debt" when unsure if the debt or the income should be considered).

supplement required documentation after consummation could raise factual questions of what income and documentation the creditor was aware of at the time of consummation, and what income and documentation were discovered only after an intensive investigation following discovery of a debt-to-income overage. The Bureau is also concerned that, in some instances a correction provision could allow loans to be deemed qualified mortgages based on post hoc documentation, notwithstanding that the creditor, in fact, would not have made the loan had it correctly calculated the consumer's debt-to-income ratio.

Although the Bureau has received requests from industry noting that it would be useful to permit corrections in situations where a creditor did not document all known income at the time of consummation, it is not clear how often this will happen in practice. Furthermore, the Bureau believes that amending the rule to allow for correction in those instances may be unnecessary because creditors could avoid such debt-to-income ratio overages by verifying additional sources of income prior to consummation, at least in loans where the debt-to-income ratio would otherwise be near the 43-percent limit.

As discussed above with respect to points and fees, the Bureau expects that, over time, creditors will develop greater familiarity with, and capabilities for, originating loans that are not qualified mortgages under the ability-to-repay requirements, as well as greater confidence in general compliance systems. As they do so, the Bureau believes creditors may relax internal debt-to-income ratio buffers that are predicated on the qualified mortgage threshold. Although the Bureau is considering whether the impacts on access to credit during the interim period (when such capabilities are being developed) may make a debt-to-income cure provision appropriate, the 43-percent debt-to-income ratio limit applies only to one category of qualified mortgages, unlike the points and fees limit, which applies to all qualified mortgages. Small creditors making qualified mortgages under § 1026.43(e)(5), (e)(6), and (f) are not subject to the 43-percent debt-to-income limit. Further, creditors of any size currently have the option of originating GSE/agency-eligible loans under the temporary qualified mortgage definition without regard to the 43-percent debt-to-income limit.[23] For this reason, the Bureau believes that a relatively small number of loans are currently affected by the debt-to-income limit.

For these reasons, the Bureau is not proposing a specific cure or correction provision related to the 43-percent debt-to-income limit for qualified mortgages under § 1026.43(e)(2) at this time. However, to aid its ongoing consideration of such provisions, the Bureau requests comment on all aspects of the debt-to-income cure or correction approaches discussed above and, in particular, requests commenters to provide specific and practical examples of where such approaches may be applied and how they may be implemented. The Bureau also requests comment on what conditions should appropriately apply to cure or correction of the qualified mortgage debt-to-income limits, including the time periods (such as the 120-day period included in the proposed points and fees cure provision) when such provisions may be available. The Bureau also requests comment on whether or how a debt-to-income cure or correction provision might be exploited by unscrupulous creditors to undermine consumer protections and undercut incentives for strict compliance efforts by creditors or assignees.

B. Request for Comment on the Credit Extension Limit for the Small Creditor Definition

Under the Bureau's 2013 Title XIV Final Rules, there are four types of exceptions and special provisions available only to small creditors:

[23] Pursuant to § 1026.43(e)(4)(ii) and (iii), the temporary GSE/agency qualified mortgage definition will sunset on the earlier of January 10, 2021 or, with respect to GSE-eligible loans, when the GSEs (or any limited-life regulatory entity succeeding the charters of the GSEs) exit government conservatorship, or, with respect to agency-eligible loans, when those agencies' qualified mortgage definitions take effect.

- A qualified mortgage definition for certain loans made and held in portfolio, which are not subject to a bright-line debt-to-income ratio limit and are subject to a higher annual percentage rate (APR) threshold for defining which first-lien qualified mortgages receive a safe harbor under the ability-to-repay rule (§ 1026.43(e)(5));[24]
- Two qualified mortgage definitions (*i.e.*, a temporary and an ongoing definition) for certain loans made and held in portfolio that have balloon-payment features, which are also subject to the higher APR threshold for defining which first-lien qualified mortgages receive a safe harbor under the ability-to-repay rule (§ 1026.43(e)(6) and (f));
- An exception from the requirement to establish escrow accounts for certain higher-priced mortgage loans (HPMLs) for small creditors that operate predominantly in rural or underserved areas (§ 1026.35(b)(2)(iii));[25] and
- An exception from the prohibition on balloon-payment features for certain high-cost mortgages (§ 1026.32(d)(1)(ii)(C)).[26]

These special rules and exceptions recognize that small creditors are an important source of non-conforming mortgage credit. Small creditors' size and relationship lending model often provide them with better ability than large institutions to assess ability-to-repay. At the same time, small creditors lack economies of scale necessary to offset the cost of certain regulatory

[24] For purposes of determining whether a loan has a safe harbor with TILA's ability-to-repay requirements (or instead is categorized as "higher-priced" with only a rebuttable presumption of compliance with those requirements), for first-lien covered transactions, the special qualified mortgage definitions in § 1026.43(e)(5), (e)(6) and (f) receive an APR threshold of the average prime offer rate plus 3.5 percentage points, rather than plus 1.5 percentage points.

[25] To meet the "rural" or "underserved" requirement, during any of the preceding three calendar years, the creditor must have extended more than 50 percent of its total covered transactions, as defined by § 1026.43(b)(1) and secured by a first lien, on properties that are located in counties that are either "rural" or "underserved," as defined by § 1026.35(b)(2)(iv). *See* § 1026.35(b)(2)(iii)(A).

[26] For loans made on or before January 10, 2016, small creditors may originate high-cost mortgages with balloon-payment features even if the creditor does not operate predominantly in rural or underserved areas, under certain conditions. *See* §§ 1026.32(d)(1)(ii)(C) and 1026.43(e)(6).

burdens. To be a small creditor for purposes of these exceptions and special provisions, the creditor must have (1) together with its affiliates, originated 500 or fewer covered transactions[27] secured by a first lien in the preceding calendar year; and (2) had total assets of less than $2 billion at the end of the preceding calendar year. As discussed in more detail below, the Bureau is requesting comment on certain aspects of the annual first-lien origination limit under the small creditor test.

These special rules for small creditors are largely based on TILA sections 129D(c) and 129C(b)(2)(E), respectively. TILA section 129D(c) authorizes the Bureau to exempt a creditor from the higher-priced mortgage loan escrow requirement if the creditor operates predominantly in rural or underserved areas, retains its mortgage loans in portfolio, and meets certain asset size and annual mortgage loan origination thresholds set by the Bureau. TILA section 129C(b)(2)(E) permits certain balloon-payment mortgages originated by small creditors to receive qualified mortgage status, even though qualified mortgages are otherwise prohibited from having balloon-payment features. The creditor qualifications under TILA section 129C(b)(2)(E) generally mirror the criteria for the higher-priced mortgage loan escrow exemption, including meeting certain asset size and annual mortgage loan origination thresholds set by the Bureau.

The Board proposed to implement TILA sections 129D(c) and 129C(b)(2)(E) before TILA rulemaking authority transferred to the Bureau. Although the creditor qualification criteria under these provisions are similar, the Board proposed to implement the provisions in slightly different ways.

To implement TILA section 129D(c), the exemption from the higher-priced mortgage loan escrow requirements, the Board proposed to limit the exemption to creditors that (1) during

[27] "Covered transaction" is defined in § 1026.43(b)(1) to mean a 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 a transaction exempt from coverage under § 1026.43(a).

either of the preceding two calendar years, together with affiliates, originated and retained servicing rights to 100 or fewer loans secured by a first lien on real property or a dwelling; and (2) together with affiliates, do not maintain escrow accounts for loans secured by real property or a dwelling that the creditor or its affiliates currently service.[28] The Board interpreted the escrow provision as intending to exempt creditors that do not possess economies of scale to escrow cost-effectively. In proposing the transaction count limit, the Board estimated that a minimum servicing portfolio size of 500 is necessary to escrow cost-effectively, and assumed that the average life expectancy of a mortgage loan is about five years. Based on this reasoning, the Board believed that creditors would no longer need the benefit of the exemption if they originated and serviced more than 100 first-lien transactions per year. The Board proposed a two-year coverage test to afford an institution sufficient time after first exceeding the threshold to acquire an escrowing capacity. The Board did not propose an asset-size threshold to qualify for the escrow exemption, but sought comment on whether such a threshold should be established and, if so, what it should be.

For the balloon-payment qualified mortgage definition to implement TILA section 129C(b)(2)(E), the Board proposed an asset-size limit of $2 billion and two alternative annual originations thresholds. The Board interpreted the qualified mortgage provision as being designed to ensure access to credit in areas where consumers may be able to obtain credit only from community banks offering balloon-payment mortgages. Accordingly, the Board proposed two alternatives for the total annual originations portion of the test: Under alternative 1, the creditor, together with all affiliates, extended covered transactions of some dollar amount or less during the preceding calendar year, whereas under alternative 2, the creditor, together with all

[28] 76 FR 11597 (Mar. 2, 2011) (2011 Escrows Proposal). The proposed exemption also would have required that, during the preceding calendar year, the creditor extended more than 50 percent of its total first-lien higher-priced mortgage loans in counties designated as rural or underserved, among other requirements.

affiliates, extended some number of covered transactions or fewer during the preceding calendar year. The Board did not propose a specific annual originations threshold in connection with TILA section 129C(b)(2)(E), but the Board sought comment on the issue.

Rulemaking authority for TILA passed to the Bureau in July 2011, before the Board finalized the above-described proposals. The Bureau considered the Board's proposals and responsive public comments before finalizing those rules in January 2013. The Bureau also conducted further analysis to try to determine the appropriate thresholds, although such effort was significantly constrained by data limitations. The Bureau ultimately adopted an annual originations limit of 500 or fewer first-lien covered transactions in the preceding calendar year and an asset-size limit of less than $2 billion, adjusted annually for inflation.[29] The Bureau believed that it would be preferable to use the same annual originations and asset-size thresholds for the qualified mortgage and escrow provisions to reflect the consistent statutory language, to facilitate compliance by not requiring institutions to track multiple metrics, and to promote consistent application of the two exemptions. The Bureau also applied these limits to the exception from the balloon-payment prohibition for high-cost loans, to the qualified mortgage definition for small portfolio creditors, and to the qualified mortgage definition for loans with balloon-payment features.

The Bureau adopted a threshold of 500 or fewer annual originations of first-lien transactions to provide flexibility and reduce concerns that the threshold in the Board's 2011 Escrows Proposal would reduce access to credit by excluding creditors that need special

[29] The higher-priced mortgage loan escrows exemption also requires that the creditor operate predominantly in rural or underserved areas. *See* § 1026.35(b)(2)(iii)(A). For loans made on or before January 10, 2016, small creditors may originate qualified mortgages, and high-cost mortgages, with balloon-payment features even if the creditor does not operate predominantly in rural or underserved areas, under certain conditions. *See* §§ 1026.32(d)(1)(ii)(C) and 1026.43(e)(6).

accommodations in light of their capacity constraints.[30] The Bureau believed that an originations limit is the most accurate means of limiting the special provisions to the class of small creditors with a business model the Bureau believes will best facilitate access to responsible, affordable credit. The Bureau also believed that an asset limit is important to preclude a very large creditor with relatively modest mortgage operations from taking advantage of a provision designed for much smaller creditors with much different characteristics and incentives, and that lack the scale to make compliance less burdensome.

Based on estimates from publicly available Home Mortgage Disclosure Act (HMDA) and call report data, the Bureau understood that the small creditor provisions as finalized would include approximately 95 percent of creditors with less than $500 million in assets, approximately 74 percent of creditors with assets between $500 million and $1 billion, and approximately 50 percent of creditors with assets between $1 billion and $2 billion. The Bureau believed these percentages were consistent with the rationale for providing special accommodation for small creditors and would be appropriate to ensure that consumers have access to responsible, affordable mortgage credit.

Consistent with the Bureau's ongoing Implementation Plan, the Bureau is seeking comment on the 500 total first-lien originations limit—and the requirement that the limit be determined for any given calendar year based upon results during the immediately prior calendar

[30] The preamble to the January 2013 Escrows Final Rule noted that the increased threshold was likely not very dramatic because the Bureau's analysis of HMDA data suggested that even small creditors are likely to sell a significant number of their originations in the secondary market and, assuming that most mortgage transactions that are retained in portfolio are also serviced in-house, the Bureau estimated that a creditor originating no more than 500 first-lien transactions per year would maintain and service a portfolio of about 670 mortgage obligations over time (assuming an average obligation life expectancy of five years). Thus, the Bureau believed the higher threshold in the January 2013 Escrows Final Rule would help to ensure that creditors that are subject to the escrow requirement would in fact maintain portfolios of sufficient size to maintain the escrow accounts on a cost-efficient basis over time, in the event that the Board's 500-loan estimate of a minimum cost-effective servicing portfolio size was too low. At the same time, however, the Bureau believed that the 500 annual originations threshold in combination with the other requirements would still ensure that the balloon-payment qualified mortgage and escrow exemptions are available only to small creditors that focus primarily on a relationship lending model and face significant systems constraints.

year. Specifically, the Bureau solicits feedback and data from (1) creditors designated as small creditors under the Bureau's 2013 Title XIV Final Rules; and (2) creditors with assets that are not at or above the $2 billion limitation but that do not qualify for small creditor treatment under the Bureau's 2013 Title XIV Final Rules because of their total annual first-lien mortgage originations. For such creditors, the Bureau requests data on the number and type of mortgage products offered and originated to be held in portfolio during the years prior to the effective date of the 2013 Title XIV Final Rules and subsequent to that date. In particular, the Bureau is interested in how such creditors' origination mix changed in light of the Bureau's 2013 Title XIV Final Rules (including, but not limited to, the percentage of loans that are fixed-rate, are adjustable-rate, or have a balloon-payment feature) and, similarly, how such creditors' origination mix changed when only considering loans originated for the purposes of keeping them in portfolio. The Bureau also solicits feedback on such small creditors' implementation efforts with respect to the Bureau's 2013 Title XIV Final Rules. The Bureau is interested in detailed descriptions of the challenges that creditors might face when transitioning from originating balloon-payment loans to originating adjustable-rate loans. Finally, the Bureau solicits comment on whether the 500 total first-lien originations limit is sufficient to serve the above-described purposes of the provision and, to the extent it may be insufficient, the reasons why it is insufficient and the range of appropriate limits.

As noted above, certain of the special provisions applicable to small creditors are limited to small creditors in "rural" or "underserved" areas. The Bureau finalized a definition of "rural" or "underserved" in the 2013 Escrows Final Rule. 78 FR 4725 (Jan. 22, 2013). The Bureau recognizes that concerns have been raised by some stakeholders that the Bureau's definition is under-inclusive and fails to cover certain counties or portions of counties that are typically thought of as rural or underserved in nature. The Bureau is considering whether to propose modifications to the definition of "rural" or "underserved" at a later date and is not requesting comment at this time on this issue.

VII. Dodd-Frank Act Section 1022(b)(2) Analysis

A. Overview

In developing the proposed rule, the Bureau has considered potential benefits, costs, and impacts.[31] The Bureau requests comment on the preliminary analysis presented below as well as submissions of additional data that could inform the Bureau's analysis of the benefits, costs, and impacts. The Bureau has consulted, or offered to consult with, the prudential regulators, the Securities and Exchange Commission, the Department of Housing and Urban Development, the Federal Housing Finance Agency, the Federal Trade Commission, the U.S. Department of Veterans Affairs, the U.S. Department of Agriculture, and the Department of the Treasury, including regarding consistency with any prudential, market, or systemic objectives administered by such agencies.

There are three main provisions in this rulemaking proposal. The first provision extends the small servicer exemption from certain provisions of the 2013 Mortgage Servicing Final Rules to nonprofit servicers that service 5,000 or fewer loans on behalf of themselves and associated nonprofits, all of which were originated by the nonprofit or an associated nonprofit. The second provision excludes certain non-interest bearing, contingent subordinate liens that meet the requirements of proposed § 1026.43(a)(3)(v)(D) ("contingent subordinate liens") from the 200-loan limit calculation for purposes of qualifying for the nonprofit exemption from the ability-to-

[31] Specifically, section 1022(b)(2)(A) of the Dodd-Frank Act calls for the Bureau to consider the potential benefits and costs of a regulation to consumers and covered persons, including the potential reduction of access by consumers to consumer financial products or services; the impact on depository institutions and credit unions with $10 billion or less in total assets as described in section 1026 of the Dodd-Frank Act; and the impact on consumers in rural areas.

repay requirements. The third provision affords creditors an option, in limited circumstances, to cure certain mistakes in cases where a creditor originated a loan with an expectation of qualified mortgage status, but the loan actually exceeded the points and fees limit for qualified mortgages at consummation ("points and fees cure").

The Bureau has chosen to evaluate the benefits, costs, and impacts of these proposed provisions against the current state of the world. That is, the Bureau's analysis below considers the benefits, costs, and impacts of the three proposed provisions relative to the current regulatory regime, as set forth primarily in the January 2013 ATR Final Rule, the May 2013 ATR Final Rule, and the 2013 Mortgage Servicing Final Rules.[32] The baseline considers economic attributes of the relevant market and the existing regulatory structure.

The main benefit of each of these proposed provisions to consumers is a potential increase in access to credit and a potential decrease in the cost of credit. It is possible that, but for these provisions, (1) financial institutions would stop or curtail originating or servicing in particular market segments or would increase the cost of credit or servicing in those market segments in numbers sufficient to adversely impact those market segments, (2) the financial institutions that would remain in those market segments would not provide a sufficient quantum of mortgage loan origination or servicing at the non-increased price, and (3) there would not be significant new entry into the market segments left by the departing institutions. If, but for these proposed provisions, all three of these scenarios would be realized, then the three proposed provisions will increase access to credit. The Bureau does not possess any data, aside from anecdotal comments, to refute or confirm any of these scenarios for any of the proposed exemptions. However, the Bureau notes that, at least in some market segments, these three

[32] The Bureau has discretion in future rulemakings to choose the relevant provisions to discuss and to choose the most appropriate baseline for that particular rulemaking.

scenarios could be realized by just one creditor or servicer stopping or curtailing originating or servicing or increasing the cost of credit. This would occur, for example, if that creditor or servicer is the only one willing to extend credit or provide servicing to this market segment (for example, to low- and moderate-income consumers), no other creditor or servicer would enter the market even if the incumbent exits, and the incumbent faces higher costs that would lead it to either increase the cost of credit or curtail access to credit.

The main cost to consumers of the proposed small nonprofit servicer and small nonprofit originator provisions is that, for some transactions, creditors or servicers will not have to provide consumers some of the protections provided by the ability-to-repay and mortgage servicing rules. The main cost of the points and fees cure provision to consumers is that a creditor could reimburse a consumer for a points and fees overage after consummation—with the creditor thereby obtaining the safe harbor or rebuttable presumption of TILA ability-to-repay compliance afforded by a qualified mortgage, and the consumer having less ability to challenge the mortgage on ability-to-repay grounds. As noted above, the Bureau does not possess data to provide a precise estimate of the number of transactions affected. However, the Bureau believes that the number will be relatively small.

The main benefit of each of these proposed provisions to covered persons is that the affected covered persons do not have to incur certain expenses associated with the ability-to-repay and mortgage servicing rules, or will not be forced either to exit the market or to curtail origination or servicing activities to maintain certain regulatory exemptions. Given the currently available data, it is impossible for the Bureau to estimate the number of transactions affected with any useful degree of precision; that is also the case for estimating the amount of monetary benefits for such covered persons.

There is no major cost of these proposed provisions to covered persons—each of the provisions is an option that a financial institution is free to undertake or not to undertake. The only potential costs for covered persons is that other financial institutions that would have complied with the ability-to-repay and mortgage servicing rules with or without the proposed provisions may lose profits to the institutions that are able to continue operating in a market segment by virtue of one of the proposed provisions. However, these losses are likely to be small and are difficult to estimate.

B. Potential Benefits and Costs to Consumers and Covered Persons

Small Servicer Exemption Extension for Servicing Associated Nonprofits' Loans

The Bureau's 2013 Mortgage Servicing Final Rules were designed to address the market failure of consumers not choosing their servicers and of servicers not having sufficient incentives to invest in quality control and consumer satisfaction. The demand for larger loan servicers' services comes from originators, not from consumers. Smaller servicers, however, have an additional incentive to provide "high-touch" servicing that focuses on ensuring consumer satisfaction. 78 FR 10695, 10845-46 (Feb. 14, 2013); 78 FR 10901, 10980-82 (Feb. 14, 2013).

The Bureau's 2013 Mortgage Servicing Final Rules provide many benefits to consumers: for example, detailed periodic statements. These benefits tend to present potential costs to servicers: for example, changing their software systems to include additional information on the periodic statements to consumers. These benefits and costs are further described in the "Dodd-Frank Act Section 1022(b)(2) Analysis" sections of the 2013 Mortgage Servicing Final Rules. 78 FR 10695, 10842-61 (Feb. 14, 2013); 78 FR 10901, 10978-94 (published concurrently).

Smaller servicers are generally community banks and credit unions that have a built-in incentive to manage their reputation with consumers carefully because they are servicing loans in communities in which they also originate loans. This incentive is reinforced if they are servicing only loans that they originate. Under current § 1026.41(e)(4)(ii), a small servicer is a servicer that either (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; or (B) is a Housing Finance Agency, as defined in 24 CFR 266.5. The definition of the term "affiliate" is the definition provided in the Bank Holding Company Act (BHCA). The rationale for the small servicer exemption is provided in the Bureau's 2013 Mortgage Servicing Final Rules. 78 FR 10695, 10845-46 (Feb. 14, 2013); 78 FR 10901, 10980-82 (published concurrently).

The proposed revision of the exemption allows a nonprofit servicer to service loans on behalf of "associated nonprofit entities" that do not meet the BHCA "affiliate" definition and still qualify as a "small servicer," as long as certain other conditions are met (for example, it has no more than 5,000 loans in its servicing portfolio). The Bureau believes nonprofit servicers typically follow the same "high-touch" servicing model followed by the small servicers described in the Dodd-Frank Act Section 1022(b)(2) Analysis in the 2013 Mortgage Servicing Final Rules. While these nonprofit servicers are not motivated by the profit incentive that motivates community banks and small credit unions, they nonetheless have a reputation incentive and a mission incentive to provide "high-touch" servicing, neither of which is diminished when they service associated nonprofits' loans. Because it is limited to entities sharing a common name, trademark, or servicemark, proposed § 1026.41(e)(4)(ii)(C) further ensures that the reputation incentive remains intact. In addition, the 5,000-loan servicing portfolio limit ensures that nonprofit servicers are still sufficiently small to provide "high-touch" servicing. Another rationale for the proposed revision of the exemption is that it would create a more level playing field for nonprofits. Currently, for-profit affiliates can take advantage of economies of scale to service their loans together, but related nonprofits cannot because they typically are not "affiliates" as defined by the BHCA.

Overall, the primary benefit to consumers of the proposed amendment to the small servicer definition is a potential increase in access to credit and a potential decrease in the cost of credit. The primary cost to consumers is losing some of the protections of the Bureau's 2013 Mortgage Servicing Final Rules. The primary benefit to covered persons is exemption from certain provisions of those rules, and the attendant cost savings of not having to comply with those provisions while still being able to achieve a certain degree of scale by taking on servicing for associated nonprofits. *See also* 78 FR 10695, 10842-61 (Feb. 14, 2013); 78 FR 10901, 10978-94 (published concurrently). There are no significant costs to covered persons.

Finally, the Bureau does not possess any data that would enable it to report the number of transactions affected, but from anecdotal evidence and taking into account the size of the nonprofit servicers that are the most likely to take advantage of this exemption, it is unlikely that there will be a significant number of loans affected each year. Several nonprofit servicers might be affected as well.

Ability-to-Repay Exemption for Contingent Subordinate Liens

The Bureau's ability-to-repay rule was designed to address the market failure of mortgage loan originators not internalizing the effects of consumers not being able to repay their loans: effects both on the consumers themselves and on the consumers' neighbors, whose houses drop in value due to foreclosures nearby.

The May 2013 ATR Final Rule added a nonprofit exemption from the ability-to-repay requirements. The rationale of that exemption is preserving low- and moderate-income consumers' access to credit available from nonprofit organizations, which might have stopped or curtailed originating loans but for this exemption. The main benefit of the exemption for consumers is in potential expansion of access to credit and a potential decrease in the cost of credit; the main cost for consumers is not receiving protections provided by the ability-to-pay rule. The May 2013 ATR Final Rule exempted only nonprofit creditors that originated 200 or fewer loans a year, based on the Bureau's belief that these institutions do internalize the effects of consumers not being able to repay their loans and that the loan limitation is necessary to prevent the exemption from being exploited by unscrupulous creditors seeking to harm consumers.

Proposed § 1026.43(a)(3)(vii) excludes contingent subordinate liens from the 200-credit extension limit for purposes of the May 2013 ATR Final Rule's nonprofit exemption. Given the numerous limitations on contingent subordinate liens, including but not limited to the 1-percent cap on upfront costs payable by the consumer—and given the 200-loan limit for other loans, the Bureau believes that the potential for creditors to improperly exploit the amended rule is low. The Bureau also believes that this exemption will allow a greater number of nonprofit creditors to originate more loans than under the current rule, or to remain in the low- and moderate-income consumer market without passing through cost increases to consumers.

Overall, the primary benefit to consumers of the proposed exclusion is a potential increase in access to credit and a potential decrease in the cost of credit. The primary cost to consumers is losing some of the protections provided by the Bureau's ability-to-repay rule. The primary benefit to covered persons is exemption from that same rule. *See* 78 FR 6407, 6555-75 (Jan. 30, 2013); ("Dodd-Frank Act Section 1022(b)(2) Analysis" part in the January 2013 ATR Final Rule); 78 FR 35429, 35492-97 (June 12, 2013) (similar part in the May 2013 ATR Final Rule). There are no significant costs to covered persons.

Finally, the Bureau does not possess any data that would enable it to report the number of transactions affected, but from anecdotal evidence and taking into account the size of the nonprofit creditors that are most likely to take advantage of this exemption, it is unlikely that there will be a significant number of loans affected each year, and it is possible that virtually no loans will be affected in the near future. Several nonprofit creditors might be affected as well, but it is possible that no nonprofit creditors will be affected in the near future.

Cure for Points and Fees Over the Qualified Mortgage Threshold

To originate a qualified mortgage, a creditor must satisfy various conditions, including the condition of charging at most 3 percent of the total loan amount in points and fees, not including up to two bona-fide discount points, and with higher thresholds for lower loan amounts. However, origination processes are not perfect and creditors might be concerned about any potential unintended errors that result in a loan that the creditor believed to be a qualified mortgage at origination but that actually was over the 3-percent points and fees threshold upon further, post-consummation review.

The three most likely responses by a creditor concerned about such inadvertent errors would be either to originate loans with points and fees well below TILA's 3-percent limit, to insert additional quality control in its origination process, or to charge a premium for the risk of a loan being deemed not to be a qualified mortgage, especially on loans with points and fees not well below TILA's 3-percent limit. The first solution is not what the Bureau, or presumably Congress, intended; otherwise the statutory limit would have been set lower than 3 percent. The second solution could result in more than the socially optimal amount of effort expended on quality control, especially since most loans will be securitized and thus re-examined shortly after origination. The savings from forgoing additional quality control might be passed through to consumers, to the extent that costs saved are marginal (as opposed to fixed) and the markets are sufficiently competitive. The third solution is, effectively, a less stark version of the first solution, with loans close to TILA's 3-percent limit still being originated, albeit at higher prices simply due to being close to the limit. Like the first potential solution, this would be an unintended consequence of the limit.

The primary potential drawback of the proposal to allow creditors to cure inadvertent points and fees errors is the risk of inappropriate exploitation by creditors. However, the conditions the Bureau has placed on the proposed cure mechanism help to ensure that creditors will not abuse this mechanism and thus that consumers are unlikely to experience negative side-effects.

One such potential gaming scenario involves a creditor originating risky loans with high points and fees while hoping to avoid a massive wave of foreclosures. In this case, the possibility of cure could be thought of as an option that the creditor could exercise to strengthen its position for foreclosure litigation, but only if the creditor foresees the wave of foreclosures. The elements of proposed § 1026.43(e)(3)(iii) requiring that the loan be originated in good faith as a qualified mortgage and that the overage be cured within 120 days after consummation should discourage this type of gaming. Another gaming scenario is a creditor that only cures overages on loans that go into foreclosure. This possibility is limited by the proposed 120-day cure window, as well as by the proposed requirement that the creditor or assignee, as applicable, maintains and follows policies and procedures for post-consummation review and refunding overages.

The primary benefit to consumers of the proposed cure provision is a potential increase in access to credit and a potential decrease of the cost of credit. Another potential benefit is that, when a creditor discovers the inadvertent points and fees overage, the creditor may reimburse the consumer for the overage. However, this is a benefit only for consumers who place greater value on being reimbursed than on the additional legal protections that a non-qualified mortgage would afford them. The primary cost to consumers is that, without the consumer's consent, a creditor could reimburse the consumer for a points and fees overage after consummation—with the creditor thereby obtaining the safe harbor (or rebuttable presumption) of TILA ability-to-repay compliance. However, the Bureau believes that the safeguards included in the proposed rule will mitigate this potential concern as creditors are unlikely to be able to game the system and thereby deprive consumers of the protections provided by the ability-to-pay rule.

The primary benefit to covered persons is being able to originate qualified mortgages without engaging in inefficient additional quality control processes, with the attendant reduction in legal risk. Some larger creditors might have sufficiently robust compliance procedures that largely prevent inadvertent points and fees overages. These creditors might lose some market share to creditors for whom this provision will be more useful. The Bureau cannot meaningfully estimate the magnitude of this effect.

Finally, the Bureau does not possess any data that would enable it to report the number of transactions affected. For some creditors, the proposed provision might save additional verification and quality control in the loan origination process for every qualified mortgage transaction that they originate[33] and/or allow them to originate loans with points and fees close to the 3-percent threshold at lower prices that do not reflect the risk of the loan inadvertently turning out not to be a qualified mortgage. The Bureau seeks comment on this issue and, in

[33] While a result of the proposed points and fees cure is that creditors have less of an incentive to perform rigorous quality control before consummation, there is also an alleviating effect. Any errors uncovered in the post-consummation review might help creditors improve their pre-consummation review by immediately pointing out areas to focus on.

particular, any detailed descriptions regarding the processes that might be simplified due to the proposed cure provision and monetary and time savings involved.

C. Impact on Covered Persons with No More Than $10 Billion in Assets

Covered persons with no more than $10 billion in assets likely will be the only covered persons affected by the two proposed exemptions regarding associated nonprofits and contingent subordinate liens: The respective loan limits of each provision virtually ensure that any creditor or servicer with over $10 billion in assets would not qualify for these two exemptions. For the third proposed provision, regarding points and fees, smaller creditors might benefit more than larger creditors. Larger creditors are more likely to have sufficiently robust compliance procedures that largely prevent inadvertent points and fees overages. Thus, this proposed provision might not benefit them as much. The third proposed provision may lead smaller creditors to extend a greater number of qualified mortgages near the 3-percent points and fees limit, to extend them for a lower price, and/or to forgo inefficient pre-consummation quality control. To the extent that possibility is realized, smaller creditors would benefit from the liability protection afforded by qualified mortgages.

D. Impact on Access to Credit

The Bureau does not believe that there will be an adverse impact on access to credit resulting from any of the three provisions. Moreover, it is possible that there will be an expansion of access to credit.

E. Impact on Rural Areas

The Bureau believes that rural areas might benefit from these three provisions more than urban areas, to the extent that there are fewer active creditors or servicers operating in rural areas than in urban areas. Thus, any creditors or servicers exiting the market or curtailing lending or servicing in rural areas—or restricting originating loans with points and fees close to the TILA 3-percent limit—might negatively affect access to credit more than similar behavior by creditors or servicers operating in more urban areas. A similar argument applies to any increases in the cost of credit.

VIII. Regulatory Flexibility Act Analysis

The Regulatory Flexibility Act (the RFA), as amended by the Small Business Regulatory Enforcement Fairness Act of 1996, requires each agency to consider the potential impact of its regulations on small entities, including small businesses, small governmental units, and small nonprofit organizations. The RFA defines a "small business" as a business that meets the size standard developed by the Small Business Administration pursuant to the Small Business Act.

The RFA generally requires an agency to conduct an initial regulatory flexibility analysis (IRFA) and a final regulatory flexibility analysis (FRFA) of any rule subject to notice-and-comment rulemaking requirements, unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. The Bureau also is subject to certain additional procedures under the RFA involving the convening of a panel to consult with small business representatives prior to proposing a rule for which an IRFA is required.

An IRFA is not required for this proposal because the proposal, if adopted, would not have a significant economic impact on any small entities. The Bureau does not expect the proposal to impose costs on covered persons. All methods of compliance under current law will remain available to small entities if the proposal is adopted. Thus, a small entity that is in compliance with current law need not take any additional action if the proposal is adopted. Accordingly, the undersigned certifies that this proposal, if adopted, would not have a significant economic impact on a substantial number of small entities.

IX. Paperwork Reduction Act

Under the Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3501 *et seq*.), Federal agencies are generally required to seek the Office of Management and Budget (OMB) approval for information collection requirements prior to implementation. The collections of information related to Regulations Z and X have been previously reviewed and approved by OMB in accordance with the PRA and assigned OMB Control Number 3170-0015 (Regulation Z) and 3170-0016 (Regulation X). Under the PRA, the Bureau may not conduct or sponsor, and, notwithstanding any other provision of law, a person is not required to respond to an information collection unless the information collection displays a valid control number assigned by OMB.

The Bureau has determined that this Proposed Rule would not impose any new or revised information collection requirements (recordkeeping, reporting, or disclosure requirements) on covered entities or members of the public that would constitute collections of information requiring OMB approval under the PRA. The Bureau welcomes comments on this determination or any other aspect of this proposal for purposes of the PRA. Comments should be submitted as outlined in the ADDRESSES section above. All comments will become a matter of public record.

List of Subjects in

12 CFR Part 1026

Advertising, Consumer protection, Credit, Credit unions, Mortgages, National banks, Reporting and recordkeeping requirements, Savings associations, Truth in lending.

Authority and Issuance

For the reasons set forth in the preamble, the Bureau proposes to amend 12 CFR part 1026 as set forth below:

PART 1026—TRUTH IN LENDING (REGULATION Z)

1. The authority citation for part 1026 continues to read as follows:

Authority: 12 U.S.C. 2601, 2603-2605, 2607, 2609, 2617, 5511, 5512, 5532, 5581; 15 U.S.C. 1601 *et seq.*

Subpart E—Special Rules for Certain Home Mortgage Transactions

2. Section 1026.41 is amended by revising paragraphs (e)(4)(ii) and (iii) to read as follows:

§ 1026.41 Periodic statements for residential mortgage loans.

*   *   *   *   *

(e) * * *

(4) * * *

(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 is a small servicer pursuant to 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 is a small servicer pursuant to 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:

*　　*　　*　　*　　*

3. Section 1026.43 is amended by revising paragraph (a)(3)(v)(D)(*1*) and the introductory text of paragraph (e)(3)(i) and adding new paragraphs (a)(3)(vii) and (e)(3)(iii) to read as follows:

§ 1026.43 Minimum standards for transactions secured by a dwelling.

(a) * * *

(3) * * *

(v) * * *

(D) * * *

(*1*) During the calendar year preceding receipt of the consumer’s application, the creditor extended credit secured by a dwelling no more than 200 times, except as provided in paragraph (a)(3)(vii) of this section;

*   *   *   *   *

(vii) Consumer credit transactions that meet the following criteria are not considered in determining whether a creditor exceeds the credit extension limitation in paragraph (a)(3)(v)(D)(*1*) of this section:

(A) The transaction is secured by a subordinate lien;

(B) The transaction is for the purpose of:

(*1*) Downpayment, closing costs, or other similar home buyer assistance, such as principal or interest subsidies;

(*2*) Property rehabilitation assistance;

(*3*) Energy efficiency assistance; or

(*4*) Foreclosure avoidance or prevention;

(C) The credit contract does not require payment of interest;

(D) The credit contract provides that repayment of the amount of the credit extended is:

(*1*) Forgiven either incrementally or in whole, at a date certain, and subject only to specified ownership and occupancy conditions, such as a requirement that the consumer maintain the property as the consumer's principal dwelling for five years;

(*2*) Deferred for a minimum of 20 years after consummation of the transaction;

(*3*) Deferred until sale of the property securing the transaction; or

(*4*) Deferred until the property securing the transaction is no longer the principal dwelling of the consumer;

(E) The total of costs payable by the consumer in connection with the transaction at consummation is less than 1 percent of the amount of credit extended and includes no charges other than:

(*1*) Fees for recordation of security instruments, deeds, and similar documents;

(*2*) A bona fide and reasonable application fee; and

(*3*) A bona fide and reasonable fee for housing counseling services; and

(F) The creditor complies with all other applicable requirements of this part in connection with the transaction.

* * * * *

(e) * * *

(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:

* * * * *

(iii) If the creditor or assignee determines after consummation that the total points and fees payable in connection with a loan 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 creditor originated the loan in good faith as a qualified mortgage and the loan otherwise meets the requirements of paragraphs (e)(2), (e)(4), (e)(5), (e)(6), or (f) of this section, as applicable;

(B) Within 120 days after consummation, the creditor or assignee refunds to the consumer the dollar amount by which the transaction's points and fees exceeded the applicable limit under paragraph (e)(3)(i) of this section at consummation; and

(C) The creditor or assignee, as applicable, maintains and follows policies and procedures for post-consummation review of loans and refunding to consumers amounts that exceed the applicable limit under paragraph (e)(3)(i) of this section.

*   *   *   *   *

4. In Supplement I to part 1026:

a. Under *Section 1026.41—Periodic Statements for Residential Mortgage Loans*:

i. Under *Paragraph 41(e)(4)(ii) Small servicer defined*, paragraph 2 is revised and paragraph 4 is added.

ii. Under *Paragraph 41(e)(4)(iii) Small servicer determination*, paragraphs 2 and 3 are revised and paragraphs 4 and 5 are added.

b. Under *Section 1026.43 – Minimum Standards for Transactions Secured by a Dwelling*:

i. New subheading *Paragraph 43(a)(3)(vii)* and paragraph 1 under that subheading are added.

ii. New subheading *Paragraph 43(e)(3)(iii)* and paragraphs 1 and 2 under that subheading are added.

The revisions read as follows:

Supplement I to Part 1026—Official Interpretations

*   *   *   *   *

Subpart E—Special Rules for Certain Home Mortgage Transactions

*   *   *   *   *

Section 1026.41—Periodic Statements for Residential Mortgage Loans

*   *   *   *   *

41(e)(4)(ii) Small servicer defined.

*   *   *   *   *

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:

*   *   *   *   *

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.

* * * * *

2. *Timing for small servicer exemption*. The following examples demonstrate when a servicer either is considered or is no longer considered a small servicer for purposes of § 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 that 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 that 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 that 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 that 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) for purposes of the small servicer determination under § 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. 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 qualifies for the small servicer exemption pursuant to § 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) for purposes of the small servicer determination under § 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 qualifies for the small servicer exemption pursuant to § 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.

*   *   *   *   *

Section 1026.43—Minimum Standards for Transactions Secured by a Dwelling

*   *   *   *   *

Paragraph 43(a)(3)(vii).

1. *Requirements of exclusion.* Section 1026.43(a)(3)(vii) excludes certain transactions from the credit extension limit set forth in § 1026.43(a)(3)(v)(D)(*1*), provided a transaction meets several conditions. The terms of the credit contract must satisfy the conditions that the transaction not require the payment of interest under § 1026.43(a)(3)(vii)(C) and that repayment of the amount of credit extended be forgiven or deferred in accordance with § 1026.43(a)(3)(vii)(D). The other requirements of § 1026.43(a)(3)(vii) need not be reflected in the credit contract, but the creditor must retain evidence of compliance with those provisions, as required by § 1026.25(a). In particular, the creditor must have information reflecting that the total of closing costs imposed in connection with the transaction is less than 1 percent of the amount of credit extended and include no charges other than recordation, application, and housing counseling fees, in accordance with § 1026.43(a)(3)(vii)(E). Unless an itemization of the amount financed sufficiently details this requirement, the creditor must establish compliance with § 1026.43(a)(3)(vii)(E) by some other written document and retain it in accordance with § 1026.25(a).

*   *   *   *   *

Paragraph 43(e)(3)(iii).

1. *Originated in good faith as a qualified mortgage.* i. The following may be evidence that a creditor originated a loan in good faith as a qualified mortgage:

A. A creditor maintains and follows policies and procedures designed to ensure that points and fees are correctly calculated and do not exceed the applicable limit under § 1026.43(e)(3)(i); or

B. The pricing for the loan is consistent with pricing on qualified mortgages originated contemporaneously by the same creditor.

ii. In contrast, the following may be evidence that a loan was not originated in good faith as a qualified mortgage:

A. A creditor does not maintain, or the creditor has, but does not follow, policies and procedures designed to ensure that points and fees are correctly calculated and do not exceed the applicable limit under § 1026.43(e)(3)(i); or

B. The pricing for the loan is not consistent with pricing on qualified mortgages originated contemporaneously by the same creditor.

2. *Policies and procedures for post-consummation review and refunding*. A creditor or assignee satisfies § 1026.43(e)(3)(iii)(C) if it maintains and follows policies and procedures for post-consummation quality control loan review and for curing (by providing a refund) errors in points and fees calculations that occur at or before consummation.

*   *   *   *   *

[THIS SIGNATURE PAGE PERTAINS TO THE AMENDMENTS TO THE 2013 MORTGAGE RULES UNDER THE TRUTH IN LENDING ACT (REGULATION Z)]

Dated: April 30, 2014

Richard Cordray

Richard Cordray,

Director, Bureau of Consumer Financial Protection.