Summary of the final rule to strengthen consumer protections for high-cost mortgages

January 10, 2013

The Consumer Financial Protection Bureau (Bureau) has issued a final rule to strengthen consumer protections for high-cost mortgages and to provide consumers with information about homeownership counseling. The new rule is effective January 10, 2014.

BACKGROUND

The Home Ownership and Equity Protection Act (HOEPA) was enacted in 1994 as an amendment to the Truth in Lending Act (TILA) to address abusive practices in refinancing and home-equity mortgage loans with high interest rates or high fees. Loans that meet HOEPA's high-cost coverage tests are subject to special disclosure requirements and restrictions on loan terms, and borrowers in high-cost mortgages have enhanced remedies for violations of the law. The provisions of TILA, including HOEPA, are implemented in the Bureau's Regulation Z.

In response to the recent mortgage crisis, Congress amended HOEPA through the Dodd Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) in order to expand the coverage of HOEPA and add protections for high-cost mortgages, including a requirement that borrowers receive homeownership counseling before obtaining a high-cost mortgage. In addition, several provisions of the Dodd-Frank Act also require or encourage consumers to obtain homeownership counseling for other types of loans. The Bureau is finalizing this rule to implement the HOEPA and homeownership counseling-related requirements.

SCOPE OF HOEPA COVERAGE

The final rule implements the Dodd-Frank Act's amendments that expanded the universe of loans potentially covered by HOEPA. Under the final rule, most types of mortgage loans secured by a consumer's principal dwelling, including purchase-money mortgages, refinances, closed-end home-equity loans, and open-end credit plans (*i.e.*, home equity lines of credit or HELOCs) are potentially subject to HOEPA coverage. The final rule retains the exemption from HOEPA coverage for reverse mortgages. In addition, the final rule adds exemptions from HOEPA coverage for three types of loans that the Bureau believes do not present the same risk of abuse as other mortgage loans: loans to finance the initial construction of a dwelling, loans originated and financed by Housing Finance Agencies, and loans originated through the United States Department of Agriculture's (USDA) Rural Housing Service section 502 Direct Loan Program.

REVISED HOEPA COVERAGE TESTS

The final rule implements the Dodd-Frank Act's revisions to HOEPA's coverage tests by providing that a transaction is a high-cost mortgage if any of the following tests is met:

- The transaction's annual percentage rate (APR) exceeds the applicable average prime offer rate by more than 6.5 percentage points for most first-lien mortgages, or by more than 8.5 percentage points for a first mortgage if the dwelling is personal property and the transaction is for less than $50,000;
- The transaction's APR exceeds the applicable average prime offer rate by more than 8.5 percentage points for subordinate or junior mortgages;
- The transaction's points and fees exceed 5 percent of the total transaction amount or, for loans below $20,000, the lesser of 8 percent of the total transaction amount or $1,000 (with the dollar figures also adjusted annually for inflation); or
- The credit transaction documents permit the creditor to charge or collect a prepayment penalty more than 36 months after transaction closing or permit such fees or penalties to exceed, in the aggregate, more than 2 percent of the amount prepaid.

The final rule also provides guidance on how to apply the various coverage tests, such as how to determine the applicable average prime offer rate and how to calculate points and fees.

RESTRICTIONS ON LOAN TERMS

The final rule also implements new Dodd-Frank Act restrictions and requirements concerning loan terms and origination practices for mortgages that fall within HOEPA's coverage test. For example:

- Balloon payments are generally banned, unless they are to account for the seasonal or irregular income of the borrower, they are part of a short-term bridge loan, or they are made by creditors meeting specified criteria, including operating predominantly in rural or underserved areas.
- Creditors are prohibited from charging prepayment penalties and financing points and fees.
- Late fees are restricted to four percent of the payment that is past due, fees for providing payoff statements are restricted, and fees for loan modification or payment deferral are banned.
- Creditors originating HELOCs are required to assess consumers' ability to repay. (Creditors originating high-cost, closed-end credit transactions already are required to

assess consumers' ability to repay under the Bureau's 2013 Ability-to-repay (ATR) Final Rule addressing a Dodd-Frank Act requirement that creditors determine that a consumer is able to repay a mortgage loan.)

- Creditors and mortgage brokers are prohibited from recommending or encouraging a consumer to default on a loan or debt to be refinanced by a high-cost mortgage.
- Before making a high-cost mortgage, creditors are required to obtain confirmation from a federally certified or approved homeownership counselor that the consumer has received counseling on the advisability of the mortgage.

OTHER COUNSELING-RELATED REQUIREMENTS

The final rule implements two additional Dodd-Frank Act homeownership counseling-related provisions that are not amendments to HOEPA.

- The final rule requires lenders to provide a list of homeownership counseling organizations to consumers within three business days after they apply for a mortgage loan, with the exclusion of reverse mortgages and mortgage loans secured by a timeshare. The final rule requires the lender to obtain the list from either a website that will be developed by the Bureau or data that will made available by the Bureau or the Department of Housing and Urban Development (HUD) for compliance with this requirement.
- The final rule implements a new requirement under TILA that creditors must obtain confirmation that a first-time borrower has received homeownership counseling from a federally certified or approved homeownership counselor or counseling organization before making a loan that provides for or permits negative amortization to the borrower.