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New Rule Summary: Amendments Relating to Small Creditors and Rural or Underserved Areas under the Truth in Lending Act

The Consumer Financial Protection Bureau (Bureau) has issued a final rule, Amendments Relating to Small Creditors and Rural or Underserved Areas under the Truth in Lending Act (Rule). The Rule, which is effective January 1, 2016, revises the Regulation Z definitions of “small creditor” and “rural area,” and makes technical changes and clarifications to other sections of Regulation Z and the related commentary. The revised definitions will affect the availability of some special provisions and exemptions to Regulation Z’s Ability-to-Repay, high-cost mortgage, and higher-priced mortgage loan (HPML) escrow requirements. However, the Rule does not revise the definition of “rural county” in Regulation Z’s HPML appraisal provisions or affect the exemption from the requirement to obtain a second appraisal for certain HPMLs.

The following summarizes the changes in the Rule and how they affect these Regulation Z requirements. Additionally, the Bureau will be updating its [Regulatory Implementation materials](#) for the Ability-to-Repay and Qualified Mortgage, Home Ownership and Equity Protection Act, and HPML Escrow Rules. This summary and the other Regulatory Implementation materials are not substitutes for the Rule. Only the Rule and its official interpretations can provide complete and definitive information regarding the Rule’s requirements.

The Rule makes the following changes to the definitions of small creditor and rural area:

- (1) **Raises the loan origination limit** for determining eligibility for small creditor status **from 500** first-lien covered transactions **to 2,000** first-lien covered transactions. Under the Rule, if a creditor and its affiliates together extended no more than 2,000 first-lien covered transactions during the preceding calendar year, the creditor may qualify as a small creditor in the current calendar year.
- (2) **Excludes loans that the creditor or its affiliate originates and keeps in its portfolio** from the loan origination limit. When determining whether a creditor and its affiliates extended more than 2,000 first-lien covered transactions, the creditor only counts first-lien covered transactions that were sold, assigned, or otherwise transferred, or were subject to a commitment to be acquired at the time of consummation. Loans held in portfolio are not counted toward the 2,000 loan origination limit, even if they are first-lien covered transactions.

- (3) **Includes the assets of an affiliate that regularly extended first-lien covered transactions** in the asset limit used to determine small creditor status. The Rule retains the asset limit of \$2 billion, adjusted annually (*e.g.*, total assets of less \$2,060,000,000 on December 31, 2014 for determining small creditor status in 2015), but requires that the creditor count not only its assets but also the assets of any affiliate that regularly extended first-lien covered transactions in the preceding calendar year. The Rule also adds language in the commentary clarifying the term “affiliate.”
- (4) **Reduces the time period used to determine whether a creditor is operating predominantly in rural or underserved areas** from any of the three preceding calendar years to the preceding calendar year. In order to be a creditor that operates predominantly in rural or underserved areas for 2016, a creditor would need to extend more than 50 percent of its total first-lien covered transactions on properties located in rural or underserved areas in calendar year 2015.
- (5) **Expands the definition of “rural area”** that a creditor uses to determine if it is operating predominantly in rural or underserved areas. The Rule expands the definition of “rural area” to include either: (a) a county that meets the current definition of a rural county; or (b) a census block that is not in an urban area as defined by the U.S. Census Bureau. The Rule adds two new safe harbors for determining whether a property is located in a rural area. A creditor will be able to rely on an automated address look up tool available on the Census Bureau’s website or on a new automated tool that will be provided on the Bureau’s website. The Rule maintains the current safe harbor for reliance on the county lists available on the Bureau’s website. The safe harbors are not the only means of demonstrating compliance, but a printout or electronic copy from the Bureau’s automated tool or the Census Bureau’s website may be used as evidence that one or more properties are located in rural areas as defined by the Rule.
- (6) **Adds a grace period** to allow a creditor that does not meet one or more of the requirements for a small creditor or a creditor that operates predominantly in rural or underserved areas in the preceding calendar year to operate, in some circumstances, as a small creditor or small creditor that operates predominantly in rural or underserved areas with respect to transactions with applications received before April 1 of the current year. If a creditor exceeded the origination limit in the preceding calendar year but did not exceed it in the calendar year preceding that one, the creditor may still qualify as a small creditor for transactions with applications received before April 1 of the current calendar year. Similarly, if a creditor exceeded the asset limit in the preceding calendar year but did not exceed it in the calendar year preceding that one, the creditor may still qualify as a small creditor for transactions with applications received before April 1 of the current calendar year. Finally, if a creditor did not extend more than 50 percent of its total covered transactions secured by first liens on properties located in areas that are rural or underserved in the preceding calendar year but did so in the calendar year preceding that one, the creditor may qualify as a creditor operating predominantly in rural or underserved areas for transactions with applications received before April 1 of the current year.

Regulation Z has special provisions and exemptions that are available only to small creditors or to small creditors that operate predominantly in rural or underserved areas. The Rule's revised definitions of small creditor and rural area affect which creditors are eligible for these special provisions and exemptions, including the following:

- (1) The provision that permits small creditor portfolio qualified mortgages that are not subject to the 43 percent debt-to-income ratio or the underwriting requirements of Appendix Q. These qualified mortgages also have a higher annual percentage rate threshold for the safe harbor from Ability-to-Repay claims (as opposed to a presumption of compliance). The revised definitions of small creditor and rural area will effectively expand the overall number of creditors that are eligible to extend small creditor portfolio qualified mortgages.
- (2) The permanent and temporary provisions for balloon-payment qualified mortgages, which permit balloon-payment features for certain loans held in portfolio without disqualifying them from qualified mortgage status and allow a higher annual percentage rate threshold for the safe harbor from Ability-to-Repay claims (as opposed to a presumption of compliance). The revised definitions of small creditor and rural area will effectively expand the overall number of creditors that are eligible to extend balloon-payment qualified mortgages under these provisions. The Rule also changes the sunset date of the temporary provision for balloon-payment qualified mortgage loans available to small creditors even if they do not operate predominantly in rural or underserved areas. The Rule will permit such balloon-payment qualified mortgages for transactions with applications received before April 1, 2016. Thus, if a creditor meets all of the requirements to be a small creditor under the Rule on January 1, 2016, but less than 50 percent of the creditor's first-lien covered transactions extended in 2015 were secured by properties located in rural or underserved areas, the creditor can still extend balloon-payment qualified mortgages for applications received before April 1, 2016.
- (3) The temporary and permanent exceptions from the prohibition on balloon-payment features for certain high-cost mortgages. The revised definitions of small creditor and rural area will effectively expand the overall number of creditors that can include balloon-payment features in certain high-cost mortgages. The Rule also changes the sunset date for the temporary exception. As with the temporary provision for balloon-payment qualified mortgages, the temporary exception regarding balloon-payment features in high-cost mortgages will apply to transactions for which an application was received before April 1, 2016.
- (4) The small creditor exception from the requirement to establish escrow accounts for certain HPMLs. Generally, a small creditor that operates predominantly in rural or underserved areas cannot rely on the exception if it maintains an escrow account for real estate- or dwelling-secured consumer credit that it or an affiliate services, unless the escrow account was established for a first-lien HPML between April 1, 2010 and January 1, 2014 or as an accommodation to a distressed consumer. To prevent a creditor that is not currently able to

rely on the escrow exception (and has been required to establish escrow accounts) from losing the ability to rely on the exception if the creditor meets the Rule's revised definitions of small creditor and rural area, the Rule also revises the conditions for qualifying for the escrow exception. A small creditor that operates predominantly in rural or underserved areas will be able to rely on the exception from the escrow requirement even if it continues to maintain escrow accounts established for first-lien HPMLs if the applications for such HPMLs were received between April 1, 2010 and January 1, 2016 or if the escrow account was established as an accommodation to a distressed consumer.