

**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:** Final rule; official interpretations.

**SUMMARY:** The Bureau of Consumer Financial Protection (Bureau) is amending certain mortgage rules issued in 2013. The final rule provides an alternative small servicer definition for nonprofit entities that meet certain requirements and amends the existing exemption from the ability-to-repay rule for nonprofit entities that meet certain requirements. The final rule also provides a cure mechanism for the points and fees limit that applies to qualified mortgages.

**DATES:** The final rule is effective on [INSERT FEDERAL REGISTER PUBLICATION DATE], except that amendment 5 to Supplement I to 12 CFR Part 1026 is effective August 1, 2015. The amendments to § 1026.43 and commentary to § 1026.43 in Supplement I to Part 1026, other than amendment 5 to Supplement I to 12 CFR Part 1026, apply to transactions consummated on or after [INSERT FEDERAL REGISTER PUBLICATION DATE]. For additional discussion regarding the effective date of the rule, see part VI, below.

**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 the Final 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).<sup>1</sup> 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, and other stakeholders. On April 30, 2014, the Bureau proposed several additional amendments to the regulations adopted by the Bureau in 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, and sought comment on additional issues. The proposal was published in the **Federal Register** on May 6, 2014. *See* 79 FR 25730 (May 6, 2014).

Specifically, the Bureau proposed three amendments to Regulation Z:

- To provide an alternative definition of the term “small servicer,” which would apply to certain nonprofit entities that service for a fee loans on behalf of other nonprofit chapters of the same organization. A “small servicer” is exempt from

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<sup>1</sup> 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, and a final rule related to the proposal was issued 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 Mortgage Servicing Rules under the Real Estate Settlement Procedures Act (Regulation X), 78 FR 10695 (Feb. 14, 2013) and the Mortgage Servicing Rules under the Truth in Lending Act (Regulation Z), 78 FR 10901 (Feb. 14, 2013) (collectively, 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).

certain requirements that apply to servicers under the Bureau’s Regulations Z (12 CFR part 1026) and X (12 CFR part 1024). The Bureau proposed this change in Regulation Z, but the change would also affect several provisions of Regulation X, which cross-reference the Regulation Z small servicer definition.

- To amend the Regulation Z ability-to-repay requirements to provide that certain non-interest bearing, 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 exceed the points and fees limit for qualified mortgages, but that meet the other requirements for being a qualified mortgage at consummation.

The Bureau is issuing a final rule with respect to these proposals. With respect to the proposals related to nonprofit servicers and the nonprofit exemption from the ability-to-repay rule, the Bureau is finalizing those provisions as proposed, with minor technical revisions to the nonprofit servicer provision. The Bureau is generally finalizing the points and fees cure provision as proposed but with certain modifications to address concerns raised by commenters.

The proposal sought comment on issues related to a possible cure for the debt-to-income ratio limit that applies to certain qualified mortgages and to the credit extension limit that applies to small creditor exemptions and special provisions in certain of the regulations adopted by the Bureau in the 2013 Title XIV Mortgage Rules. Those issues are not addressed in this final rule. The Bureau is considering comments submitted on those issues and whether to address those issues in a future rulemaking.

## **II. Background**

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.<sup>2</sup> 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.<sup>3</sup>

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.<sup>4</sup> 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. Those rules included the January 2013 ATR Final Rule and the 2013 Mortgage Servicing Final Rules. Pursuant to the Dodd-Frank Act, which permitted a maximum of one year for implementation, the January 2013 ATR Final Rule and the 2013 Mortgage Servicing Final Rules had effective dates of January 10, 2014.

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<sup>2</sup> 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).

<sup>3</sup> 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.).

<sup>4</sup> See section 1400(c) of the Dodd-Frank Act, 15 U.S.C. 1601 note.

Concurrent with the January 2013 ATR Final Rule, on January 10, 2013, the Bureau issued proposed amendments to the rule (the January 2013 ATR Proposal), which the Bureau adopted on May 29, 2013 (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 provisions adopted by the Bureau in the 2013 Mortgage Servicing Final Rules and the May 2013 ATR Final Rule in the summer and fall of 2013.<sup>5</sup> This final rule 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.

### **III. Comments**

On May 6, 2014, the Bureau published a proposal in the **Federal Register** to amend certain aspects of the Regulation Z ability-to-repay/qualified mortgage requirements and servicing rules. *See* 79 FR 25730 (May 6, 2014). The comment period closed on June 5, 2014.<sup>6</sup> In response to the proposal, the Bureau received more than 40 comments from consumer groups, creditors, industry trade associations, and others. As discussed in more detail below, the Bureau has considered these comments in adopting this final rule.

### **IV. Legal Authority**

The Bureau is issuing this final 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,

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<sup>5</sup> 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).

<sup>6</sup> The proposal also sought comment on additional issues relating to qualified mortgage debt-to-income ratio overages and the credit extension limit for the small creditor definition. The comment period for those aspects of the proposal closed on July 7, 2014. As noted above, the Bureau is not addressing those issues through this final rule.

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's) 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.<sup>7</sup>

#### *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 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

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<sup>7</sup> 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).

terms that reasonably reflect their ability to repay the loans and that are understandable and not unfair, deceptive, or 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 for the class of transactions";
- 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; are necessary and appropriate to effectuate the purposes of the ability-to-repay and residential mortgage loan origination requirements; prevent circumvention or evasion thereof; or 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.<sup>8</sup> Notably, the authority granted by section 1405(b) applies to “disclosure requirements” generally, and is not limited to a

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<sup>8</sup> “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).

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

## **V. Section-by-Section Analysis**

### *Section 1026.41 Periodic Statements for Residential Mortgage Loans*

#### *41(e) Exemptions*

#### *41(e)(4) Small Servicers*

#### *The Bureau’s Proposal*

The Bureau proposed to revise the scope of the exemption for small servicers in § 1026.41(e)(4)(ii) and incorporated by cross-reference in certain provisions of Regulation X. The proposal would have added an alternative definition of small servicer in § 1026.41(e)(4)(ii)(C), 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 proposal also

would have made conforming changes to § 1026.41(e)(4)(ii) and (iii) and associated commentary.

Currently, Regulation Z exempts small servicers from certain mortgage servicing requirements. Small servicers are defined in Regulation Z § 1026.41(e)(4)(ii), and Regulation X also relies on this same definition. Regulation Z exempts small servicers from the requirement to provide periodic statements for residential mortgage loans.<sup>9</sup> Regulation X exempts small servicers from: (1) certain requirements relating to obtaining force-placed insurance;<sup>10</sup> (2) the provisions relating to general servicing policies, procedures, and requirements;<sup>11</sup> and (3) certain requirements and restrictions relating to communicating with borrowers about, and evaluation of loss mitigation applications.<sup>12</sup>

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 its 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).<sup>13</sup> Generally, under current

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<sup>9</sup> 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).

<sup>10</sup> 12 CFR 1024.17(k)(5) (prohibiting purchase of force-placed insurance in certain circumstances).

<sup>11</sup> 12 CFR 1024.30(b)(1) (exempting small servicers from §§ 1024.38 through 41, except as otherwise provided under § 1024.41(j), as discussed in note 12, *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.

<sup>12</sup> 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).

<sup>13</sup> 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

§ 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, § 1026.41(e)(4)(iii) provides exceptions, which include mortgage loans that are 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.<sup>14</sup>

Prior to issuing the proposal related to this final rule, the Bureau learned that certain nonprofit entities may, for a fee, service loans for another nonprofit entity that is part of the same larger network of nonprofits. These nonprofits are separately incorporated but operate under mutual contractual obligations to serve the same charitable mission, and use a common name, trademark, or servicemark. Such 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). Groups of nonprofit entities that are associated with one another in the described manner may consolidate servicing activities to achieve economies of scale necessary to service loans cost-effectively, and such cost 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 may be unable to qualify for the small servicer exemption, unlike their for-profit counterparts.

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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).

<sup>14</sup> Section 1026.41(e)(4)(ii) also excludes from consideration reverse mortgage transactions and mortgage loans secured by consumers' interests in timeshare plans for purposes of determining whether a servicer qualifies as a small servicer.

To address these concerns, the Bureau proposed to revise the scope of the small servicer exemption in Regulation Z § 1026.41 that is also applicable to certain provisions of Regulation X. The Bureau believed that the ability of such nonprofit entities to consolidate servicing activities may be beneficial to consumers—to the extent servicing cost savings are passed on to consumers or lead to increased credit availability—and may outweigh the consumer protections provided by the servicing rules to those consumers affected by the proposal. The Bureau was 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 servicing rules provide important protections for consumers, the Bureau was 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 would qualify for the proposed § 1026.41(e)(4)(ii)(C) exemption. Furthermore, the Bureau believed these nonprofit entities, because of their scale and community-focused lending programs, have other 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.

Accordingly, the proposal would have added 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) would have provided 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)(I) would have defined the term “nonprofit entity,” for purposes of

proposed § 1026.41(e)(4)(ii)(C), to mean an entity having a tax exemption ruling or determination letter from the Internal Revenue Service (IRS) under section 501(c)(3) of the Internal Revenue Code of 1986 (IRC). *See* 26 U.S.C. 501(c)(3); 26 CFR 501(c)(3)-1. Proposed § 1026.41(e)(4)(ii)(C)(2) would have defined “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 also proposed technical changes to § 1026.41(e)(4)(iii), which would have addressed the timing of the small servicer determination and also excludes certain loans from being counted toward the 5,000-loan limitation. The proposed changes would have added 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 inserted 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 have provided 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.

In addition, the Bureau proposed technical changes to comment 41(e)(4)(ii)-2 and proposed to add comment 41(e)(4)(ii)-4 to parallel existing comment 41(e)(4)(ii)-2 (that would have addressed 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 have clarified that there would be two elements to satisfying the nonprofit small servicer definition in proposed § 1026.41(e)(4)(ii)(C). First, the comment would have clarified 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 would be made separately without consideration of the number of loans serviced by another associated nonprofit entity. Second, the comment would have explained that the nonprofit entity would have to 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) would have to be the entity to which the mortgage loan obligation was initially payable (that is, the originator of the mortgage loan). The comment would have explained that a nonprofit entity would not be 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 have provided two examples to demonstrate the application of the small servicer definition under § 1026.41(e)(4)(ii)(C).

The Bureau also proposed, along with some other clarifying and technical changes, to revise existing comment 41(e)(4)(iii)-3 to 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 also not considered for determining whether a servicer (together with any affiliates) services 5,000 or fewer mortgage loans or for determining whether a servicer is servicing only mortgage loans that it (or an affiliate) owns or originated. Finally, the Bureau proposed a new comment 41(e)(4)(iii)-4 to 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) also would not be considered 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 for determining whether a nonprofit entity is servicing only

mortgage loans that it or an associated nonprofit entity originated. The comment would have provided examples to illustrate the rule.

For the reasons discussed below, the Bureau is adopting § 1026.41(e)(4)(ii)(C) and (iii) and the accompanying commentary as proposed, with minor technical revisions.

*Comments*

The Bureau received comments on the proposed amendment to the small servicer definition from a nonprofit servicer, consumer groups, credit union trade associations, and a mortgage trade association. Commenters generally favored the proposed provision, but they suggested certain revisions to the proposed nonprofit small servicer definition and expressed concerns about possible evasion.

In the proposal, the Bureau sought comment on whether the definition of a nonprofit entity should contain additional criteria regarding the nonprofit's activities or the loan's features or purposes. Consumer group commenters expressed concern that the proposed definition of nonprofit entity might allow evasion. These groups urged the Bureau to add language and clarification to avoid abuse by dishonest nonprofits. These commenters stated that some entities may cease to comply with § 501(c)(3) of the IRC, but could still have a tax exemption ruling or determination letter from the IRS until the IRS formally revoked its status. The commenters stated that a nonprofit would remain eligible for the exemption despite blatant evidence that the entity was not a bona fide nonprofit. These commenters urged the Bureau to require the nonprofit entity to be a bona fide nonprofit operating in compliance with IRC § 501(c)(3).

Consumer group commenters also expressed concern with proposed comment 41(e)(4)(ii)-4, which would provide that each associated nonprofit entity may service no more than 5,000 loans under the nonprofit small servicer definition. These commenters requested that

the Bureau publicly state that it would monitor use of the exemption to prevent abuse by servicers that service more than 5,000 loans.

Credit union trade associations generally supported expansion of the small servicer exemption. However, they requested the exemption be expanded further to exempt credit unions. They noted that Federal and State chartered credit unions are typically designated as tax-exempt under IRC §§ 501(c)(1) and (14), respectively. In support of such an expansion, one credit union trade association noted that some credit unions that would otherwise qualify for the existing small servicer definition under § 1024.41(e)(4)(ii)(A) are disqualified because of ownership stakes in credit union service organizations (CUSOs).

*Final Rule*

For the reasons set forth below, the Bureau is adopting as proposed § 1026.41(e)(4)(ii) and (iii) and associated commentary. The Bureau finds that the potential benefits to consumers that may result from nonprofit entities consolidating servicing activities outweigh the consumer protections provided by the servicing rules to the affected consumers. The Bureau believes that the entities that qualify for the exemption under the nonprofit small servicer definition have other incentives to provide high levels of customer contact and information, which lends further support to the exemption.

The Bureau considered comments requesting the addition of a bona fide qualifier to the nonprofit small servicer definition but has not adopted this approach in the final rule. A bona fide requirement is unnecessary because the nonprofit small servicer definition is more limited than the existing small servicer definition and is narrowly tailored to prevent evasion. Specifically, the nonprofit small servicer definition would require that a nonprofit entity service only loans for which it or an associated nonprofit entity is the creditor. This is in contrast to the

existing small servicer exemption under § 1026.41(e)(4)(ii)(A), which applies to entities that service loans for which it or an affiliate is the creditor *or assignee*. To satisfy the nonprofit small servicer definition, an associated nonprofit entity must be the creditor on the loan. In addition, to meet the nonprofit small servicer definition, the “associated nonprofit entities,” as defined in § 1026.41(e)(4)(ii)(C)(2), must by agreement operate using a common name, trademark, or servicemark to further and support a common charitable mission or purpose. As such, nonprofit entities that operate in a manner that is inconsistent with the group’s common charitable purpose—or a group of associated nonprofits that operates without a charitable purpose—would not satisfy the nonprofit small servicer definition. Although the final rule does not include a bona fide nonprofit qualifier, the Bureau will monitor use of the nonprofit small servicer exemptions and consider any changes to the definition, as appropriate.

The Bureau has not expanded the nonprofit small servicer definition to cover credit unions designated as tax-exempt under IRC §§ 501(c)(1) and (14), as requested by some credit union and credit union trade association commenters.<sup>15</sup> The Bureau believes that credit unions and their affiliates are likely to have greater capacity to comply with the full mortgage servicing rules than those nonprofit entities that are covered by the nonprofit small servicer definition. The commenters did not provide any data to support an expansion of the exemption to credit unions.

#### *Legal Authority*

The Bureau is adopting an exemption from the periodic statement requirement under TILA section 128(f) for certain small servicers pursuant to its authority under TILA section

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<sup>15</sup> The Bureau previously considered, but declined to adopt, a broad exemption for credit unions in adopting the original small servicer definition in § 1026.41(e)(4)(ii)(A) in the 2013 Final Mortgage Servicing Rule. See 78 FR 10901, 10976 (Feb. 14, 2013). Subsequently, in clarifying the small servicer definition in the July 2013 Mortgage Servicing Final Rule, the Bureau considered concerns that affiliate relationships between certain credit unions and credit union service organizations (CUSOs) may prevent the credit unions and CUSOs from qualifying for the small servicer exemption, but declined to adopt such an exemption because the comments were beyond the scope of the rulemaking. See 78 FR 44685, 44694 (July 24, 2013). The Bureau finds that a broad exemption for credit unions is outside the scope of this rulemaking as well.

105(a) and (f) and Dodd-Frank Act section 1405(b).

For the reasons discussed above, the Bureau finds that the 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 finds 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 finds that such nonprofits may consolidate servicing functions in an associated nonprofit entity to provide more cost-effectively this high level of customer contact and otherwise to comply with applicable regulatory requirements. As noted, 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 finds that the nonprofit small servicer definition facilitates compliance with TILA by allowing nonprofit small servicers to consolidate servicing functions, without losing status as a small servicer, to service loans more cost-effectively in compliance with applicable regulatory requirements.

In addition, consistent with TILA section 105(f) and in light of the factors in that provision, the Bureau finds that requiring nonprofit entities servicing 5,000 or fewer loans (including those serviced on behalf of associated nonprofits, for all of which that servicer or an associated nonprofit is the creditor) 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 finds 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 finds that the nonprofit small servicer definition 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 finds that exempting nonprofit small servicers from the requirements of TILA section 128(f) is in the interest of consumers and in the public interest.

As noted above, 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 amending the small servicer definition in Regulation Z, the Bureau is also effectively amending 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 exempting 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 finds that the nonprofit small

servicer definition would ensure that 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 finds that the nonprofit small servicer definition 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 adopting 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's Proposal*

The Bureau proposed to amend the nonprofit small creditor exemption from the ability-to-repay rule that is set forth in § 1026.43(a)(3)(v)(D). 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 and meet certain additional requirements.

The proposal would have excluded certain subordinate-lien transactions from the 200-credit extension limit. For the reasons set forth below and in the proposal, the Bureau is finalizing this provision as proposed.

Currently, § 1026.43(a)(3)(v)(D) provides an exemption from the ability-to-repay rule if the creditor and the loan meet certain criteria. First, the creditor must have a tax exemption ruling or determination letter from the IRS under section 501(c)(3) of the IRC. Second, the creditor may not have extended credit secured by a dwelling more than 200 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 be 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.

As noted in the proposal, 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 expressed concern that they may be forced to curtail their subordinate-lien programs or more generally limit their lending activities to avoid exceeding the 200-credit extension limit. In particular, these entities 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.

In light of these concerns, the Bureau proposed to amend § 1026.43(a)(3)(v)(D)(I) to exclude certain subordinate liens from the 200-credit extension limit determination. Specifically, the Bureau proposed to add § 1026.43(a)(3)(vii), which would have provided that consumer credit transactions that meet the following criteria would not be considered in determining whether a creditor meets the credit extension limit in § 1026.43(a)(3)(v)(D)(I): (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 have clarified 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 have further clarified 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 includes 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 would have largely mirrored a provision and accompanying comment that was adopted as part of the Bureau's rule integrating the pre-consummation disclosure requirements of TILA and RESPA (2013 TILA-RESPA Final Rule), effective August 1, 2015. *See* 78 FR 79729 (Dec. 31, 2013). That provision, which was adopted in both Regulation X, at § 1024.5(d) (by cross-reference), and Regulation Z, at § 1026.3(h), provides a partial exemption from the disclosure requirements for loans that meet criteria that largely mirror those in proposed § 1026.43(a)(3)(vii). As noted in the proposal, that exemption was intended to describe criteria associated with certain housing assistance loan programs for low- and moderate-income persons. The Bureau believed the same criteria for the partial exemption from the 2013 TILA-RESPA Final Rule would describe the class of transactions that might appropriately be excluded from the 200-credit extension limit in the ability-to-repay exemption for nonprofits and that defining a single class of transactions for

purposes of § 1024.5(d), § 1026.3(h), and § 1026.43(a)(3)(vii) might facilitate compliance for creditors.

*Comments*

The Bureau received comments on the proposed revisions to the nonprofit creditor exemption from consumer groups, credit union trade associations, and one nonprofit creditor. Commenters generally favored the proposed provision but raised concerns about the scope and interpretation of the provisions.

The nonprofit creditor commenter generally supported the proposal but requested certain revisions and clarifications. First, the commenter expressed concern with the requirement in proposed § 1026.43(a)(3)(vii)(D) that, to be excluded from the 200-credit extension limit, the credit contract provide that repayment be forgiven or deferred. Specifically, that commenter expressed concern that a subordinate lien that defers repayment, but for less than 20 years, does not meet the criteria for the exclusion from the credit extension limit under proposed § 1026.43(a)(3)(vii)(D)(2). The commenter did not indicate whether its exemption status or the status of any other nonprofit creditor might be jeopardized if this provision were finalized, nor did it provide a specific justification for loosening the deferment period. Second, the nonprofit creditor requested that the repayment criteria be revised or commentary added to clarify that the provisions in the credit contract may provide for repayment where a borrower defaults on or refinances an accompanying first-lien mortgage without jeopardizing the loan's exemption status. Third, the nonprofit creditor commenter expressed concerns that the 200-credit extension limit discourages expansion and consolidation among nonprofit creditors. The commenter stated that the existing extension limit complicates mortgage sale transactions to its banking partners,

but did not suggest any specific number of credit extensions that would be an appropriate limit for the nonprofit creditor exemption.

Consumer group commenters generally supported adoption of the proposal but two consumer group commenters suggested that the Bureau should occasionally examine subordinate liens to ensure that any fees charged are bona fide. Credit union trade association commenters suggested that the Bureau expand the nonprofit exemption to include both Federal and State credit unions.

*Final Rule*

For the reasons discussed in the proposal, and in light of the comments received, the Bureau is adopting the revision to § 1026.43(a)(3)(v)(D), the addition of § 1026.43(a)(3)(vii), and comment 43(a)(3)(vii)-1 as proposed.

The Bureau considered whether to relax the deferment period required by § 1026.43(a)(3)(vii)(D)(2) but has not adopted such a change in the final rule. The Bureau believes that relaxing the deferment period may create a risk of consumer harm with respect to the excluded subordinate liens. As noted in the proposal, the exclusion is narrowly tailored to accommodate subordinate-liens that both reduce a consumer's monthly mortgage obligations and allow the consumer to control whether and when repayment is triggered, for at least 20 years. Reducing that period where the consumer controls repayment increases risks to consumers. The 20-year deferment requirement also serves to discourage use of the exclusion as a means of evasion of the ability-to-repay rule. Moreover, the nonprofit commenter did not assert that the 20-year deferment period required by § 1026.43(a)(3)(vii)(D)(2) would presently or foreseeably jeopardize its exemption status (or the exemption status of any other nonprofit creditor). Finally, as noted above, § 1026.43(a)(3)(vii) largely mirrors a provision that was adopted as part of the

Bureau's 2013 TILA-RESPA Final Rule. The Bureau does not, at this time, believe there is a basis for amending the exclusion from that rule and is concerned that maintaining two separate exclusion regimes would create undue regulatory burden.

In addition, the Bureau considered whether the rule or commentary should specify that the credit contract may provide for repayment where a consumer defaults on or refinances an accompanying first-lien mortgage. However, the Bureau does not believe that such a provision is necessary. The exclusion criteria do not bar such provisions, nor would such provisions be inconsistent with the proposed criteria. The Bureau is concerned that revising § 1026.43(a)(3)(vii) or adding commentary expressly to permit such standard contract terms could call into question the effect of other standard contract terms providing for acceleration, such as for nonpayment of property taxes, on a loan's status under the exclusion. As a result, addressing these provisions might necessitate amending the commentary to cover a much more exhaustive list of what is prohibited or permitted.

The Bureau also considered the request that it increase or remove the 200-credit extension limit from the § 1026.43(a)(3)(v)(D) nonprofit exemption altogether. The Bureau has determined that it would be inappropriate to do so because it believes that nonprofit creditors that originate more than 200 dwelling-secured transactions in a year (excluding the transactions described in § 1026.43(a)(3)(vii)) generally have the resources necessary to comply with the TILA ability-to-repay requirements. In the absence of information that suggests that the rationale behind the extension limit is no longer appropriate, the Bureau has not increased the extension limit.

As noted above, consumer group commenters suggested that subordinate liens should be examined occasionally to determine whether any charges imposed are bona fide. The Bureau

intends to monitor the mortgage market to ensure that the nonprofit creditor exemption does not become a means for evasion of the ability-to-repay requirements.

As also noted above, some commenters suggested that the nonprofit creditor exemption be expanded to cover State and Federal credit unions. The Bureau notes that, in adopting the nonprofit creditor exemption in the May 2013 ATR Final Rule, the Bureau considered, but declined to adopt, an exemption for entities that are designated nonprofit organizations under sections 501(c)(1) and (14) of the IRC. *See* 78 FR 35429, 35468 (June 12, 2013). Commenters did not present any information that would suggest that the Bureau should reconsider its decision in the May 2013 ATR Final Rule. Thus the Bureau lacks a sufficient basis to adopt an expanded exemption as requested by the credit union trade associations.

#### *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 above, the Bureau concludes that the amendment to the § 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 concludes that the amendment to 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 amendment to the exemption, the Bureau concludes 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 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 also considered the factors in TILA section 105(f) and concludes that, for the reasons discussed above, the amendment to the exemption is appropriate under that provision. For the reasons discussed above, the Bureau concludes that the 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 concludes that the 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 concludes that the 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 concludes that, on balance, the 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 Bureau’s Proposal*

The Bureau proposed to permit a creditor or assignee to cure an excess over the qualified mortgage points and fees limit under defined conditions. Those conditions included that the creditor originated the loan in good faith as a qualified mortgage, that the creditor or assignee refunds the overage within 120 days of consummation, and that the creditor or assignee maintains and follows policies and procedures for post-consummation review of loans and refunding to consumers of such points and fees overages. For the reasons discussed below, the Bureau is finalizing the proposed cure provision but is making certain adjustments to address concerns raised by commenters.

Section 1411 of the Dodd-Frank Act added TILA section 129C(a) 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(a). TILA section 129C(b) further: provides that the ability-to-repay requirements are presumed to be met if the loan is a qualified mortgage; sets certain product-feature and underwriting requirements for qualified mortgages (including limits on points and fees); and gives the Bureau authority to revise, add to, or subtract from these requirements.<sup>16</sup> Section 1026.43(e)(3), which implements the statutory points and fees limits for qualified mortgages, provides that the up-front points and fees charged in connection with a qualified mortgage must not exceed 3 percent of the total loan amount, with higher thresholds specified for various categories of loans below \$100,000. Pursuant to § 1026.32(b)(1), points and fees are the “fees or charges that are known at or before

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<sup>16</sup> 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.”

consummation.” The current rule does not provide a mechanism for curing points and fees overages that are discovered after consummation.

As noted in the proposal, the Bureau understands that some creditors seeking to originate and some secondary market participants seeking to purchase qualified mortgages may establish buffers, set at a level below the applicable points and fees limit in § 1026.43(e)(3)(i), to avoid inadvertently exceeding those limits. Creditors may simply refuse to extend mortgage credit to consumers whose loans would exceed the buffer threshold (even though such loans, if under the applicable Regulation Z points and fees limit, would otherwise be qualified mortgages), due to the creditors’ concerns about the potential liability attending loans originated under the general ability-to-repay standard, the ability to sell those loans into the secondary market, or the risk of repurchase demands from the secondary market if the applicable qualified mortgage points and fees limit is later found to have been exceeded. Alternatively, creditors may charge more for loans exceeding the buffer threshold (even if those loans are under the applicable Regulation Z points and fees limit for qualified mortgages). The proposal noted the Bureau’s concerns that access to credit might be negatively affected where such buffers are established.

Because of these concerns about access to credit, the Bureau proposed § 1026.43(e)(3)(iii), which would have provided 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, provided: (A) the creditor originated the loan in good faith as a qualified mortgage and the loan otherwise meets the requirements for a qualified mortgage in § 1026.43(e)(2), (e)(4), (e)(5), (e)(6), or (f), 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 § 1026.43(e)(3)(i); 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 § 1026.43(e)(3)(i).

In conformance with proposed § 1026.43(e)(3)(iii), the Bureau also proposed to amend § 1026.43(e)(3)(i) to add the introductory phrase “[e]xcept as provided in paragraph (e)(3)(iii) of this section.” That conforming change would have specified that the cure provision in § 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). Proposed comment 43(e)(3)(iii)-1 would have provided examples of evidence that a creditor originated a loan in good faith as a qualified mortgage and examples of evidence that a loan was not originated in good faith as a qualified mortgage. Proposed comment 43(e)(3)(iii)-2 would have provided guidance on the policies and procedures requirement. In addition to these specific proposals, the Bureau requested comment on whether a post-consummation points and fees cure should be permitted, and whether different, additional, or fewer conditions should be imposed upon its availability.

*Comments*

Industry commenters, including trade associations, large and small creditors, and secondary market purchasers, unanimously supported permitting a cure for points and fees overages. Industry commenters noted that the complex nature of the points and fees calculation and the potential liability associated with non-qualified mortgages have caused some creditors to impose operational buffers on points and fees that are well under the limits in the rule. These commenters also noted that it is not uncommon for investors and originators to disagree on the

interpretation of parts of the points and fees calculation, which may impede the sale of some loans in the secondary market. One large industry trade association cited the definition of “bona fide discount point,” which depends in part on whether “the interest rate without any discount” exceeds a certain threshold, as an area of industry uncertainty in the points and fees calculation that could lead to different interpretations.

Industry commenters stated that creditors that are uncertain of the qualified mortgage status of loans near the applicable points and fees limit may overprice the risk of the loan, passing on the costs of legal uncertainty to the consumer. Those commenters stated that, as a result, consumers receive loans on less favorable terms than they would otherwise receive or may be ineligible for credit. These commenters stated that the points and fees cure would provide creditors the opportunity to achieve precise compliance after consummation, which in turn would allow creditors to approve more loans, or provide loans at a lower cost to, consumers at the boundaries of the points and fees limits under the rule.

Industry commenters also generally stated that the proposed cure provision would incentivize robust post-consummation quality control and audit procedures in a way that would benefit both creditors and consumers. Creditors would benefit by being afforded the opportunity to achieve precise compliance and allow loans to flow smoothly into the secondary market, while consumers would benefit by receiving cure payments. A nonprofit commenter that promotes asset-building policies for low- and middle-income families also supported the proposed points and fees cure. This commenter noted that, for smaller loans subject to the tiered points and fees limits, any change in total costs agreed to at or near consummation may cause the loan to cross from one limit tier to another.

Some consumer group commenters, including two large national consumer groups, strongly opposed the proposed cure provision. These commenters generally stated that the proposal would do more harm to consumers than good and was unnecessary, contrary to Congressional intent, and without evidentiary foundation. Consumer group commenters that generally opposed the cure provision stated that it could incentivize inaccurate pre-consummation points and fees calculations. For example, these commenters warned that loan originators and processors could face pressure to close loans and to overlook problems before closing in the belief that they can be cured post-consummation. To these commenters, the cure would encourage the lending industry to be less vigilant, less accurate and, for some, less honest, in marketing, disclosures, and underwriting practices. Consumer group commenters also objected to the proposal's provision allowing a cure by refunding nothing more than the overage to the consumer.

Some consumer group commenters argued that the cure is unnecessary because of the regulations' limited impact on access to credit. Two large national consumer group commenters stated that the qualified mortgage points and fees limits are not actually restricting access to credit or increasing the cost of credit. Those commenters cited a lack of data to support the Bureau's assertions about the effect of the points and fees limits on access to credit. The commenters stated that, if it had such data, the Bureau should adjust the qualified mortgage standards rather than permit a cure. The commenters argued that the mortgage industry restricts or expands access to credit based on perceptions of credit risk and profitability and not on the impact of consumer protection rules.

The commenters asserted that, although current concerns are about access to credit, creditors will loosen their standards in order to increase their market share—just as they did

before the recent financial crisis. Some consumer group commenters also noted that the Dodd-Frank Act was adopted to prevent the type of irresponsible lending that led to the financial crisis, and that each exception the Bureau adds to the qualified mortgage rule weakens the restraints the Dodd-Frank Act imposed. These commenters argued that the cure will harm consumers by depriving them of otherwise available legal remedies.

Consumer group commenters also stated that the secondary market had already taken action to address repurchase concerns. The commenters noted that, to the extent that credit is tight due to the risk of repurchase demands from the secondary market, the government-sponsored enterprises (GSEs) have announced a set of revised quality review policies and a right to fix documentation problems that will reduce creditors' exposure to repurchase demands. Other consumer group commenters, including a large national nonprofit, generally supported the cure but urged the Bureau to include greater protections for consumers in the final rule. Similarly, the consumer groups that generally opposed the cure commented that, if the Bureau adopts a points and fees cure provision, it should provide greater consumer protections. These commenters made several suggestions to increase consumer protections in the final rule, including: a sunset date for the right to cure; cutting off the right to cure upon notice from the consumer of an overage and other similar events; and requiring creditors or assignees to provide a cure payment that is more than the overage itself. These suggestions are discussed more fully, below.

#### *Final Rule*

For the reasons discussed below, the Bureau is adopting the cure provision for points and fees overages in § 1026.43(e)(3)(iii) and (iv). The Bureau is finalizing the cure provision substantially as proposed but with some modifications based on comments received. The final

cure provision provides bright-line rules to incentivize creditors to ease current points and fees buffers (and, in turn, increase access to responsible, affordable mortgage credit) while, at the same time, limiting the ability and incentives for creditors to engage in careless pre-consummation points and fees calculations or otherwise misuse the cure. In addition to certain clarifying changes, the final rule makes the following adjustments from the proposal:

- Sunsets the cure after January 10, 2021;
- Eliminates the condition that the creditor originate the loan in “good faith” as a qualified mortgage (discussed below in the section-by-section analysis of § 1026.43(e)(3)(iii)(A));
- Increases the cure period from 120 days to 210 days after consummation (discussed below in the section-by-section analysis of § 1026.43(e)(3)(iii)(B));
- Cuts off the ability to cure upon one or more of the following occurrences: the consumer’s institution of a legal action in connection with the loan; the creditor, assignee, or servicer’s receipt of the consumer’s written notice that the loan’s points and fees exceeded the qualified mortgage limit; or the consumer becoming 60 days past due on the legal obligation (discussed below in the section-by-section analysis of § 1026.43(e)(3)(iii)(B)); and
- Requires the creditor or assignee to also pay interest to the consumer on the dollar amount by which the points and fees exceed the qualified mortgage limit, for the period from consummation until the cure payment is made to the consumer (discussed below in the section-by-section analysis of § 1026.43(e)(3)(iv)).

The cure will only be available for transactions consummated on or after the effective date of this final rule and on or before the sunset date.

The Bureau concludes that the cure provision will ease current market uncertainties and, as a result, may increase consumers' access to affordable credit in the near term. As explained in the proposal, 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. Where a creditor originated a loan with the expectation of qualified mortgage status, the Bureau believes the consumer likely received the benefit of qualified mortgage treatment by receiving lower overall pricing. For this reason, the Bureau concludes that a cure provision, if appropriately limited, could reflect the expectations of both consumers and creditors at consummation and could increase access to credit for consumers seeking loans at the margins of the points and fees limits. A limited cure provision should also promote consistent pricing within the qualified mortgage range by decreasing the market's perceived need for higher pricing at the margins of the points and fees limits. The cure provision should also promote stability in the market by limiting the need for repurchase demands that may otherwise be triggered without the cure. In addition, the Bureau notes that the cure provision will encourage some creditors to undertake or strengthen rigorous post-consummation review of loans and consequently result in consumers receiving cure payments that would not have been received absent a cure provision.

At the same time, and as stated in the proposal, the Bureau expects that, over time, creditors will develop greater confidence in compliance systems and also with originating loans that are not qualified mortgages under the general ability-to-repay standard. As this occurs, creditors should be able to relax internal buffers on points and fees that are predicated on the qualified mortgage threshold and to provide consistent pricing for qualified mortgages that are at the margin of the points and fees limits. Additionally, the risk of repurchase demands based on points and fees overages should decrease with experience. For these reasons, the cure provision

finalized in § 1026.43(e)(3) contains a sunset date of January 10, 2021. This sunset date is also the general sunset date for the temporary qualified mortgage definition for loans eligible for purchase or guarantee by the GSEs or certain Federal agencies pursuant to § 1026.43(e)(4). As creditors' confidence increases and market conditions stabilize, creditors should become less reliant on points and fees buffers. The Bureau concludes that this sunset will provide sufficient time for creditors to develop confidence in compliance systems for regulatory requirements and for economic and market conditions to stabilize.

As noted above, consumer group commenters argued that the cure provision could encourage the lending industry to be negligent or reckless. The Bureau notes that the final cure provision has been carefully calibrated to incentivize creditors to ease current buffers (which should in turn increase access to responsible, affordable mortgage credit), while limiting the ability and incentives for creditors to abuse the cure. The Bureau acknowledges that a cure provision could allow some creditors to conduct inaccurate pre-consummation points and fees calculations and that the cure provision would operate to limit legal remedies for some consumers who might later bring ability-to-repay claims. However, the Bureau concludes that the safeguards described more fully below, such as limiting the cure period to a short and finite period after consummation, cutting off the ability to cure upon the occurrence of certain events (including the consumer filing a lawsuit in connection with the loan), and requiring creditors to pay interest on the points and fees overages, will appropriately limit the incentives and opportunity for misuse of the cure. Market forces (such as repurchase demands), concerns about litigation risk, and the costs of administering a post-consummation cure, will also limit the extent to which creditors may be incentivized to misuse the cure provision.

The Bureau also believes that, in most cases, the cure provision will align the loan terms with the expectations of the creditor and the consumer: The creditor likely believed the loan was a qualified mortgage when it originated the loan and, assuming buffers that affect pricing at the margins are removed, the consumer likely received more affordable qualified mortgage pricing because of the creditor's belief that the loan was a qualified mortgage. If a cure is effectuated, the consumer will also receive a monetary cure payment for the points and fees overage. For these reasons, the Bureau concludes that allowing a points and fees cure as structured in this final rule will benefit consumers.

*Legal Authority*

The Bureau is adopting the points and fees cure provision in § 1026.43(e)(3) 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. In addition, because revised § 1026.43(e)(3) permits creditors to cure non-compliance with the general qualified mortgage points and fees limits up to 210 days after consummation, the Bureau also adopts revised § 1026.43(e)(3) pursuant to its authority under section 105(a) and (f) of TILA. Each of these authorities is discussed in turn below.

For the reasons discussed herein, the Bureau concludes that revised § 1026.43(e)(3) is warranted under TILA section 129C(b)(3)(B)(i) because the limited post-consummation cure provision is necessary and proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of section 129C of TILA, and also necessary and appropriate to facilitate compliance with section 129C of TILA. For example, the Bureau concludes that the limited post-consummation cure provision will facilitate

compliance with TILA section 129C by encouraging rigorous, post-consummation quality control loan reviews that will, over time, improve the origination process.

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 the purposes of TILA. For the reasons discussed below, the Bureau concludes 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 concludes that a 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 applicable limit under the rule. 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 to the extent some creditors will not make loans near the points and fees limits due to concerns about inadvertently exceeding that limit, or will make more expensive loans near the limit. This would be contrary to the purposes of TILA, which include ensuring that responsible, affordable mortgage credit remains available to consumers. *See* 15 U.S.C. 1639b(a)(1). The Bureau also concludes that a limited post-consummation cure provision will facilitate compliance with TILA section 129C by encouraging rigorous, 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 concludes that a limited points and fees cure provision is appropriate under that provision. The Bureau concludes that the exemption, as limited by the final rule, is appropriate for all affected consumers,

specifically, those seeking loans at the margins of the points and fees limits whose access to credit may be affected adversely without the exemption. Similarly, the Bureau concludes that the 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 concludes that, on balance, the exemption will not undermine the goal of consumer protection or increase the complexity or expense of (or otherwise hinder) the credit process. 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 concludes such potential losses are outweighed by the potentially increased access to responsible, affordable credit, an important benefit to consumers. The Bureau concludes 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.

43(e)(3)(iii)

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

*The Bureau's Proposal*

As noted above, proposed § 1026.43(e)(3)(iii)(A) would have required, as a condition of curing a points and fees overage, that the loan was originated 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) (*i.e.*, the requirements to be a qualified mortgage), as applicable. The Bureau also proposed comment 43(e)(3)(iii)-1, which would have provided examples of evidence that a loan was originated in good faith as a qualified mortgage, and examples of circumstances that would evidence that a loan was not originated in good faith as a qualified mortgage. The Bureau proposed to limit the cure provision to loans originated in good faith as a qualified mortgage to

ensure that the cure provision is available only in cases of inadvertent errors in the origination process and to prevent creditors from misusing the cure provision by intentionally exceeding the points and fees limits. However, the Bureau sought comment on whether the good faith element of proposed § 1026.43(e)(3)(iii)(A) is necessary in light of the other proposed limitations on the cure provision. The Bureau also sought comment on the proposed examples in comment 43(e)(3)(iii)-1.

For the reasons discussed below, the final rule does not contain an express requirement that the loan was originated in good faith as a qualified mortgage. Rather, as finalized, § 1026.43(e)(3)(iii)(A) requires, as a condition of curing a points and fees overage, that the loan otherwise meets the criteria for a qualified mortgage in § 1026.43(e)(2), (e)(4), (e)(5), (e)(6), or (f), as applicable.

*Comments*

Industry commenters argued for removal of the “good faith” requirement for exercising a points and fees cure. These commenters argued that a good faith standard is too subjective and likely to create grounds for expensive litigation. They also stated it is unnecessary because of other limitations on the cure provision, among other reasons.

First, industry commenters stated that the subjective nature of good faith would have the unintended consequence of limiting industry’s use of the points and fees cure. They noted that the good faith requirement cannot be satisfied by objectively reviewing a loan file post-consummation. One GSE commenter noted that the good faith requirement would require an assignee to maintain copies of the creditor’s business records, which may present evidentiary issues if introduced in court by an assignee in future litigation.

Second, industry commenters argued that the good faith requirement could lead to expensive litigation. For example, one large industry trade association argued that, even if a creditor had acted in good faith, because good faith may be a jury question, it would be difficult to get claims dismissed. The commenter argued that the same is true with respect to the two examples of good faith in the proposed commentary. Whether a creditor had appropriate policies and procedures, or whether a loan was priced as a qualified mortgage, may be a jury question, thus prospective litigation costs (and other risks) would militate against reducing current buffers.

Third, industry commenters argued that the good faith requirement is unnecessary to discourage bad behavior by a creditor. These commenters stated that assignees' contractual remedies provide sufficient incentives for good behavior by creditors. They also argued that the good faith requirement is unnecessary in light of the cure provision's other requirements, including that the loan otherwise comply with all applicable qualified mortgage provisions. These commenters also noted the availability of other methods of ensuring the cure provision is not abused, such as bringing actions for unfair or deceptive acts or practices.

Fourth, industry commenters requested that, if the good faith requirement is retained, the commentary should provide more definitive statements as to what constitutes good faith. For example, one GSE commenter stated that avoiding subjective terms such as "consistent" or "contemporaneously" would be useful. Similarly, one large bank trade association argued that stating that a particular factor "is" evidence of good faith rather than merely saying it "may be" evidence of good faith would provide greater clarity and certainty that the good faith standard was met. A GSE commenter also noted that it is unclear what percentage of loans originated by the creditor should be reviewed to determine consistency (*i.e.*, whether review of all loans is required or whether some lower percentage is sufficient). Two State industry trade associations

stated that the term “contemporaneously” would not take into account the different types of loans and loan features that affect pricing more than proximity in time.

The consumer group commenters who generally opposed a points and fees cure stated that if the final rule permits a cure it must require good faith both in the loan’s origination as a qualified mortgage and in exercising the cure itself. These commenters stated that, without a good faith requirement for the cure, creditors and assignees could selectively cure loans only when they feared a challenge to the creditor’s compliance with the ability-to-repay rule or when the creditor wanted to sell a loan on the secondary market. These commenters argued that the final rule should make clear that curing some loans selectively, or otherwise using the cure provision to cut off a consumer’s attempt to seek a remedy, indicates the mortgage holder is attempting to evade compliance, rather than making a good faith attempt to comply, with the qualified mortgage rule.

Consumer group commenters also noted that allowing creditors to exercise the right to cure for loans that were not originated in good faith as qualified mortgages would defeat the consumer protection purpose of the ability-to-repay rule. Several such commenters suggested that the magnitude of the points and fees error is relevant to determining whether the loan was originated in good faith as a qualified mortgage; the larger the amount of the overage, the less likely it is that the loan was originated in good faith as a qualified mortgage loan. Consumer group commenters were also concerned that, absent a good faith requirement, the cure would become a license for careless underwriting.

#### *Final Rule*

Section 1026.43(e)(3)(iii)(A) of the final rule provides that, as a condition of exercising the cure, the loan must meet the requirements of § 1026.43(e)(2), (e)(4), (e)(5), (e)(6), or (f), as

applicable. The final rule does not expressly require that the loan was originated in good faith as a qualified mortgage. As noted above, the Bureau largely expects creditors and assignees to use the cure provision in cases of inadvertent errors in the origination process. In addition, the Bureau concludes that meeting the other requirements to be a qualified mortgage is a sufficient proxy for the loan being originated with the expectation of qualified mortgage status, and eliminating the good faith requirement provides a bright-line rule that gives certainty to creditors and assignees. The final rule contains additional mechanisms to prevent creditors from misusing the cure provision, such as cutting off the ability to cure before the consumer becomes seriously delinquent on payments; upon the institution of an action by the consumer related to the loan; or upon notice of the points and fees overage from the consumer. The Bureau is not finalizing comment 43(e)(3)(iii)-1 as proposed, because it is not adopting the good faith requirement as part of the cure provision.

As discussed, the Bureau intends the cure to provide certainty to the market until it has gained experience with the qualified mortgage rules and points and fees calculations in particular. Good faith—or its absence—may be clear in some situations, but in other situations it may only be determined based on an analysis of the facts and circumstances of the particular case. The Bureau recognizes that such case-by-case determinations would not provide the certainty that the cure provision is intended to provide. This uncertainty could deter creditors and assignees from relying on the cure provision and, instead, incentivize creditors to maintain current points and fees buffers. To the extent creditors do not rely on the cure provision, its intended purpose of increasing access to credit or decreasing the cost of credit would not be realized. Moreover, the Bureau expects that secondary market forces may impose many of the same restraints as the good faith requirement would have imposed.

Consumer group commenters argued that, without the good faith requirement, the cure provision could lead to careless or willful pre-consummation points and fees overages. However, the Bureau believes that if the loan must meet all other qualified mortgage requirements at consummation, the final rule should largely prevent creditors from engaging in careless calculations and limit use of the cure to loans that were originated with the expectation of qualified mortgage status. The Bureau further concludes that concerns about litigation risk, repurchase demands, and the administrative costs associated with curing points and fees overages will discourage creditors from conducting inaccurate pre-consummation calculations or intentionally exceeding the applicable points and fees limit for qualified mortgages.

In addition, and as explained more fully below in the section-by-section analysis of § 1026.43(e)(3)(iii)(B), the Bureau is adopting other safeguards to ensure that creditors and assignees have the proper incentives not to engage in careless or willful pre-consummation overages. These safeguards include cutting off the right to cure when the consumer files a lawsuit in connection with the loan, when the consumer gives written notice of the points and fees overage, or when the consumer becomes 60 days past due on the legal obligation. Additionally, the final rule requires that the cure payment to consumers include interest in addition to the overage amount, to guard against abuse of the cure provision. *See* the section-by-section analysis of § 1026.43(e)(iv). Finally, the Bureau notes that a repeated pattern of inappropriate underwriting could be viewed as a potential violation of other Federal consumer protection laws. The Bureau intends to monitor the use of the cure provision for potential abuses and will consider changes to the rule to prevent abuses, as appropriate.

The Bureau considered but is not adopting an approach that takes into account the magnitude of the points and fees overage because the Bureau does not believe the magnitude of

an overage alone indicates an intent to abuse the cure provision. Moreover, the Bureau believes creditors are sufficiently motivated to avoid large points and fees overages because they generally seek to avoid HOEPA's 5 percent points and fees threshold. *See* § 1026.32(a)(1)(ii). As noted, this final rule contains more targeted safeguards to prevent abuse of the cure provision.

The Bureau also considered comments from consumer groups who urged that the rule require the cure to be executed in good faith and who expressed concern that the cure provision could allow creditors and assignees to selectively cure overages only after problems develop with the loan. These comments are addressed in the section-by-section analysis of § 1026.43(e)(3)(iii)(C), below.

#### *43(e)(3)(iii)(B)*

##### *The Bureau's Proposal*

As noted above, proposed § 1026.43(e)(3)(iii)(B) would have required the creditor or assignee, within 120 days after consummation, to refund the overage amount (*i.e.*, the dollar amount by which the transaction's points and fees at consummation exceeded the applicable limit under paragraph § 1026.43(e)(3)(i)) to effect a points and fees cure. The proposal solicited comment on whether the rule should provide a longer or shorter cure period and, if a longer period, whether additional cure limitations should apply beyond those in the proposal. For example, the Bureau solicited comment on whether a cure should be permitted where a consumer has already instituted an action or provided the creditor or assignee with written notice of the error. For the reasons discussed below, the Bureau is adopting § 1026.43(e)(3)(iii)(B) with modifications that extend the cure period to 210 days after consummation and automatically terminate the cure period upon certain events.

##### *Comments*

Although one large creditor and one trade association supported the proposed 120-day cure period, most industry commenters argued in favor of extending that period. Several trade associations recommended increasing the number of days after consummation, including one State trade association that favored a period up to one year after consummation. Most of those commenters supported a cure period of at least 180 days after consummation to allow many creditors to maintain existing systems for review.

To supplement the proposed 120-day cure period, a large creditor, a GSE, and two trade associations recommended also permitting cure within a certain period (*e.g.*, 60, 120, or 270 days) after the purchase of the loan on the secondary market. Those commenters generally argued that the proposed cure period is too short to allow assignees opportunities for loan compliance review; for example, the GSE commenter, which favored a period extending 270 days after loan purchase, stated that its average time between consummation and a completed loan review in 2013 was approximately nine months—and that this timeframe might increase due to additional testing related to the January 2013 and May 2013 ATR Final Rules.

Industry commenters also supported extending the cure period from the time the error is discovered. Two GSEs recommended 120 days after discovery, while three trade associations endorsed a cure period of 60 days after discovery, not to exceed one year from consummation. The GSEs noted that TILA section 130(b) and current § 1026.31(h) of Regulation Z already have cure periods that extend from the time that an error is discovered. One of the GSEs also advocated allowing a loan to be cured so long as the creditor or assignee provides notice to the consumer within the cure period, with the actual cure payment coming within a reasonable time (*e.g.*, 30 days) after that notice. One trade association suggested that, to encourage more cure payments to consumers, a cure should be permitted even if the overage is discovered after the

standard cure period, so long as the consumer has not already instituted a legal action and the creditor or assignee makes a larger cure payment.

Some commenters also suggested different forms of payment, which could have some implications for the timing of the cure payment. A GSE commenter advocated for having the cure payment made to the consumer through a check or an automated clearing house (ACH) transfer to the consumer's checking or savings account. A regional trade association commenter urged that consumers and creditors should have an option to directly apply the cure payment to the relevant loan obligation.

Consumer group commenters supported the proposal to limit the cure period to a fixed period after consummation. Those commenters favored the proposal over a time period based on discovery of the overage, citing drawn-out uncertainty and additional litigation that a discovery-based period would cause. The consumer group commenters stated that a cure period running from discovery of the error, rather than from consummation, would allow creditors or assignees to intentionally cure only loans in which problems have arisen by claiming that the overage had been discovered only then.

Because the cure affords creditors and assignees qualified mortgage protection where there was a defect in the points and fees calculation at the time of consummation, consumer group commenters also stated that the cure period should automatically terminate upon certain events (“cut-off events”) to preserve consumers’ potential ability-to-repay claims. These commenters noted that TILA’s cure provision has similar cut-off events.<sup>17</sup> Consumer group commenters recommended that the cut-off events should include a consumer defaulting on the loan. The commenters viewed a default within the first few months after consummation as

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<sup>17</sup> The general TILA section 130(b) cure provision applies to TILA violations. Given that TILA does not require all loans to be qualified mortgages, TILA section 130(b) is not directly applicable to the qualified mortgage points and fees limit.

strong evidence that the loan may have violated ability-to-repay underwriting requirements. Consumer group commenters also advocated other cut-off events, broadly including various means for consumers to assert legal remedies regarding the loan, *e.g.*, filing a lawsuit, exercising a right of rescission, and complaining to a regulator. Consumer group commenters specifically recommended that cut-off events include a consumer or regulator notifying a creditor or assignee of a points and fees error; the commenters noted that, if a consumer or regulator discovers the error before the creditor or assignee cures, that is a possible indication that the creditor or assignee lacks robust loan review procedures or is attempting to exploit the cure provision in bad faith.

The Bureau also received some comments from industry groups regarding cut-off events. A GSE commenter argued that, for consumers struggling to make payments on their loans, cut-off events may deprive them of an opportunity to review their loans for points and fees overages and potentially receive a cure payment that could assist them in making loan payments. A trade association argued that cutting off the cure upon the consumer's notice of a points and fees error would encourage every consumer to send such notices automatically for every loan to strengthen their litigation claims.

#### *Final Rule*

The Bureau is adopting § 1026.43(e)(3)(iii)(B) with modifications extending the cure period to 210 days after consummation and automatically terminating the cure period upon certain enumerated events. As finalized, § 1026.43(e)(3)(iii)(B) provides that the cure is only available if the creditor or assignee makes the cure payment described in § 1026.43(e)(3)(iv) to the consumer within 210 days after consummation and prior to the occurrence of any of the following events: (1) the consumer's institution of an action in connection with the loan; (2) the

creditor, assignee, or servicer receiving the consumer’s written notice that the transaction’s total points and fees exceed the applicable limit under § 1026.43(e)(3)(i); or (3) the consumer becoming 60 days past due on the legal obligation. The cure payment amount under the final rule is discussed below in the section-by-section analysis of § 1026.43(e)(3)(iv).

The Bureau concludes that limiting the cure to a short and specific period after consummation, and automatically terminating that cure period upon certain events, will provide certainty to the market and increase access to credit, while also curbing the potential for abuses of the cure provision. For example, the limited cure period will discourage creditors from intentionally or recklessly originating loans with high points and fees and then waiting as long as possible to see if certain loans become riskier—with the expectation that, if they do, the creditor will use the cure provision selectively to help avoid legal liability on those loans. With a limited cure period, such a scenario becomes riskier and less attractive to creditors. At the same time, the Bureau recognizes that, if the cure period is too limited, creditors and assignees will be deterred from relying on the cure provision in lieu of maintaining current buffers near the qualified mortgage points and fees limits, which would hinder the intended effect of increasing access to affordable credit.

The Bureau concludes that a cure period limited to 210 days after consummation will address the concerns of many industry commenters. Prior to the proposal, the Bureau’s initial outreach to industry stakeholders suggested that a 120-day period after consummation would be consistent with industry’s existing systems for quality control review. However, as discussed above, most industry commenters that suggested a specific cure time period stated that 180 days after consummation would be more consistent with current practices for post-consummation review. It is not clear whether all such commenters considered the administrative time required

to process a cure payment once a points and fees overage has been identified, or whether those commenters were instead focused solely on current timelines for completing post-consummation loan audits. One GSE commenter suggested that 30 days is a reasonable amount of time for creditors or assignees to process and execute a cure payment to the consumer.

The Bureau is finalizing a cure period of 210 days after consummation, which generally provides 180 days for post-consummation points and fees reviews and an additional 30 days to process and provide cure payments to consumers. The Bureau is not adopting a cure period that could extend beyond 210 days after consummation because, as explained above, an extended cure period would increase the potential for abusing the cure. Moreover, a cure period running from a loan's purchase or an overage's discovery would provide less encouragement for rigorous and prompt loan review and would likely delay cure payments to consumers.

The Bureau is also adopting new comment 43(e)(3)(iii)-1 to provide additional clarification regarding the 210-day cure period. The comment provides that the creditor or assignee, as applicable, complies with § 1026.43(e)(3)(iii)(B) if it makes the cure payment described in § 1026.43(e)(3)(iv) to the consumer within 210 days after consummation and prior to the occurrence of any of the cut-off events described in § 1026.43(e)(3)(iii)(B)(1) through (3). A creditor or assignee, as applicable, does not comply with § 1026.43(e)(3)(iii)(B) if the cure payment is made to the consumer more than 210 days after consummation or after the occurrence of any of the events in § 1026.43(e)(3)(iii)(B)(1) through (3). In response to public comments suggesting different forms of payment, comment 43(e)(3)(iii)-1 also provides that the cure payment may be made by any means mutually agreeable to the consumer and the creditor or assignee, as applicable, or by check. This provision in comment 43(e)(3)(iii)-1 clarifies that the consumer and creditor or assignee (as applicable) may agree to any method of making the cure

payment to the consumer. For example, as discussed below in the section-by-section analysis of § 1026.43(e)(3)(iv), the consumer and the creditor or assignee may agree to apply the cure payment towards the loan’s unpaid principal balance. This provision in comment 43(e)(3)(iii)-1 also clarifies that the creditor or assignee (as applicable) may make the cure payment to the consumer by check without the agreement of the consumer. As such, comment 43(e)(3)(iii)-1 further provides that, if the cure payment is made by check, the creditor or assignee complies with § 1026.43(e)(3)(iii)(B) if the check is delivered or placed in the mail to the consumer within 210 days after consummation.

The Bureau further concludes that the cure period should terminate automatically upon certain enumerated cut-off events, particularly given the expanded cure period provided in the final rule. Specifically, those cut-off events are: (1) the consumer’s institution of any action in connection with the loan; (2) the creditor, assignee, or servicer receiving the consumer’s written notice that the transaction’s total points and fees exceed the applicable limit under § 1026.43(e)(3)(i); or (3) the consumer becoming 60 days past due on the terms of the legal obligation. As discussed below, the Bureau concludes that these limitations will help protect consumers, curb potential abuse of the cure provision, and incentivize the creditor or assignee to detect and make cure payments as early as possible. At the same time, the Bureau expects that the enumerated cut-off events will not substantially hinder the cure provision’s intended effect of increasing access to affordable credit. The Bureau anticipates that the cut-off events will occur relatively infrequently and should not unduly deter creditors and assignees from relying on the cure provision.

*Institution of any action.* The Bureau concludes that creditors and assignees should not be permitted to cure defects in points and fees calculations after the consumer’s institution of a

legal action in connection with the loan. The Bureau is concerned that allowing a points and fees cure after the action is instituted would permit creditors and assignees to misuse the cure provision. The Bureau concludes that cut-off events should not be limited to actions related to the ability-to-repay rules. Any litigation by the consumer so early in the loan's term is a signal of potential problems and suggests that the consumer likely values the right to litigate more than the limited cure payment, regardless of whether the claim is based specifically on the ability-to-repay rules or sounds in another legal theory. Moreover, consumers in litigation are well-positioned to negotiate compensation in settlement of the litigation, and so are unlikely to be harmed by cutting off the cure.<sup>18</sup> Accordingly, § 1026.43(e)(3)(iii)(B)(I) cuts off the ability to cure upon the consumer's institution of any action in connection with the loan.

The Bureau declines to cut off the ability to cure upon a regulator's institution of an action in connection with the loan. While such an action so early in the loan's term may also be a signal of potential problems with the loan, a regulator instituting an action does not indicate whether an individual consumer values a potential litigation claim more than the limited cure payment. Legal action by a regulator may be connected to a vast number of loans for which the regulator is unable to determine whether each consumer would prefer to receive a cure payment.

*Written notice of overage.* The Bureau also concludes that creditors and assignees should not be permitted to cure defects in points and fees calculations after a consumer provides notice of a points and fees overage to the creditor, assignee, or servicer. The Bureau is concerned that cutting off the cure period only when a consumer files legal action would encourage disputes to be taken to court prematurely. Such an approach would be inefficient and would increase costs for both consumers and creditors.

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<sup>18</sup> While the institution of any action by the consumer in connection with the loan will cut off the ability to cure a points and fees overage and thus prevents the loan from being a qualified mortgage, nothing in this rule precludes the negotiated settlement of claims otherwise permitted by law.

Unlike the cut-off event related to the institution of legal action described above, the notice cut-off event is triggered only where the consumer specifically gives notice that points and fees exceed the applicable limit, and not by notice of any defect with the loan more generally. The Bureau concludes this approach is appropriate to prevent consumers from inadvertently cutting off the ability to cure (and therefore potentially forfeiting cure payments) and also to provide a bright-line rule. The Bureau assumes that most consumers who have identified points and fees overages and are concerned about preserving their ability-to-repay litigation rights will be represented by counsel and will be able to make tactical decisions about forgoing a cure payment to strengthen their ability-to-repay claims.<sup>19</sup> These consumers may prefer to delay litigation if, for example, they are seeking a loan modification and are unsure if legal action will ultimately be necessary or if they believe additional investigation is necessary before bringing suit. Accordingly, § 1026.43(e)(3)(iii)(B)(2) cuts off the ability to cure upon the creditor, assignee, or servicer receiving written notice from the consumer that the transaction's total points and fees exceed the applicable limit under § 1026.43(e)(3)(i). Given that many consumers communicate with their servicers regarding their loans, § 1026.43(e)(3)(iii)(B)(2) specifically provides that notice of an overage to the servicer, in addition to the creditor and assignee, cuts off the ability to cure. For the reasons discussed above regarding cutting off the cure upon initiation of an action, the Bureau also concludes that notice of a points and fees overage from a regulator (rather than the consumer) should not cut off the cure period.

A trade association commenter argued that a cut-off event based on an overage notice would incentivize all consumers to send such overage notices for every loan. The Bureau notes, however, that the notice cut-off event in the final rule is a concept similar to that in TILA section

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<sup>19</sup> As noted above, nothing in this rule precludes the negotiated settlement of claims otherwise permitted by law. *See supra* note 18.

130(b), and the Bureau is unaware of evidence that TILA section 130(b) has led to significant problems.

*60 days past due.* The Bureau concludes that consumers who are 60 days behind on their loans should generally be able to preserve potential ability-to-repay claims. Consumer group commenters broadly recommended that a consumer’s default should cut off the cure period, but they did not elaborate on the types of default or periods of delinquency. The Bureau believes that, if cut-off events are too broad, creditors and assignees will be deterred from relying on the cure provision in lieu of maintaining current buffers near the qualified mortgage points and fees limits. The Bureau concludes that including any and all consumer defaults as cut-off events does not strike an appropriate balance between promoting affordable credit with the cure and protecting litigation rights for consumers most likely to benefit from them.

A widely-used threshold for defining “serious” delinquencies is 90 days.<sup>20</sup> The Bureau believes that a loan becoming seriously delinquent within the first 210 days after consummation raises concerns that the loan violates ability-to-repay requirements. *See, e.g.,* comment 43(c)(1)-1.ii.B.1 (“the consumer’s default on the loan a short time after consummation” may be evidence that a creditor’s ability-to-repay determination was not reasonable or in good faith). For this reason, the cure is not permitted for seriously delinquent loans. Further, the Bureau is concerned that permitting cure of a points and fees overage when a loan is already near the point of serious delinquency could incentivize abuse of the cure provision. Therefore, § 1026.43(e)(iii)(3)(B)(3) cuts off the ability to cure upon a payment becoming 60 days past due.

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<sup>20</sup> See, e.g., Freddie Mac, January 2014 U.S. Economic & Housing Market Outlook —Taking the Temperature of the Markets 1 (Jan. 16, 2014), available at [http://www.freddiemac.com/finance/pdf/Jan\\_2014\\_public\\_outlook.pdf](http://www.freddiemac.com/finance/pdf/Jan_2014_public_outlook.pdf); Fannie Mae, Monthly Summary 4 tbl. 9 (June 2014), available at <http://www.fanniemae.com/resources/file/ir/pdf/monthly-summary/063014.pdf>.

The Bureau is also adopting new comment 43(e)(3)(iii)-2 to provide additional clarification regarding the 60 days past due threshold. The comment provides that, for purposes of § 1026.43(e)(3)(iii)(B)(3), “past due” means the failure to make a periodic payment (in one full payment or in two or more partial payments) sufficient to cover principal, interest, and, if applicable, escrow under the terms of the legal obligation. Other amounts, such as any late fees, are not considered for this purpose. For purposes of § 1026.43(e)(3)(iii)(B)(3), a periodic payment is 30 days past due when it is not paid on or before the due date of the following scheduled periodic payment and is 60 days past due when, after already becoming 30 days past due, it is not paid on or before the due date of the next scheduled periodic payment. For purposes of § 1026.43(e)(3)(iii)(B)(3), the creditor or assignee may treat a received payment as applying to the oldest outstanding periodic payment.

The commentary provides an example to illustrate the meaning of 60 days past due for purposes of § 1026.43(e)(3)(iii)(B)(3). The example assumes a loan is consummated on October 15, 2015, that the consumer’s periodic payment is due on the 1st of each month, and that the consumer timely made the first periodic payment due on December 1, 2015. For purposes of § 1026.43(e)(3)(iii)(B)(3), the consumer is 30 days past due if the consumer fails to make a payment (sufficient to cover the scheduled January 1, 2016 periodic payment of principal, interest, and, if applicable, escrow) on or before February 1, 2016. For purposes of § 1026.43(e)(3)(iii)(B)(3), the consumer is 60 days past due if the consumer then also fails to make a payment (sufficient to cover the scheduled January 1, 2016 periodic payment of principal, interest, and, if applicable, escrow) on or before March 1, 2016. For purposes of § 1026.43(e)(3)(iii)(B)(3), the consumer is not 60 days past due if the consumer makes a payment (sufficient to cover the scheduled January 1, 2016 periodic payment of principal,

interest, and, if applicable, escrow) on or before March 1, 2016. This is consistent with the general industry accounting practice of crediting a received payment by applying it to the oldest outstanding periodic payment.<sup>21</sup>

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

*The Bureau's Proposal*

Proposed § 1026.43(e)(3)(iii)(C) and proposed comment 43(e)(3)(iii)-2 would have provided that, as a condition of curing a points and fees overage, 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). For the reasons set forth below, the Bureau is finalizing § 1026.43(e)(3)(iii)(C), with certain clarifying changes. The Bureau is not finalizing the substance of proposed comment 43(e)(3)(iii)-2 but is finalizing new comment 43(e)(3)(iii)-3 to provide additional guidance on the post-consummation policies and procedures requirement in § 1026.43(e)(3)(iii)(C).

*Comments*

A State industry trade association and a nonprofit organization supported the post-consummation policies and procedures requirement as appropriate. However, several industry commenters expressed doubts about the requirement.

Some industry commenters were not certain of the scope of the proposed requirement. For example, one national industry association asked whether a post-consummation review of all loans was required and noted that the cost of such a requirement would be prohibitive. A large

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<sup>21</sup> See, e.g., Fannie Mae, *Security Instruments*, <https://www.fanniemae.com/singlefamily/security-instruments> (last visited October 15, 2014) (security instruments for various states but with a uniform covenant that payments shall be applied to each periodic payment in the order in which it became due, such as Fannie Mae & Freddie Mac, *California Single Family Uniform Instrument 4*, available at [https://www.fanniemae.com/content/legal\\_form/3005w.doc](https://www.fanniemae.com/content/legal_form/3005w.doc); Fannie Mae & Freddie Mac, *New York Single Family Uniform Instrument 5*, available at [https://www.fanniemae.com/content/legal\\_form/3033w.doc](https://www.fanniemae.com/content/legal_form/3033w.doc)).

creditor noted that the proposed cure period of 120 days would not provide sufficient time for post-consummation reviews of a significant number of loans.

Other industry commenters, including a large creditor and an association of large creditors, argued that the post-consummation policies and procedures requirement introduced a subjective element into the cure procedure and that the resulting uncertainty would make the cure provision less usable by creditors. A GSE commenter stated that, in addition to being subjective, the requirement is not necessary. This commenter argued that the mere existence of a limited cure period would provide a powerful incentive for creditors to maintain and follow post-consummation review policies and procedures.

While consumer group commenters generally did not focus on the post-consummation policies and procedures requirement, they addressed related issues by insisting that the cure itself must be made in good faith. As noted in the section-by-section analysis of § 1026.43(e)(3)(iii)(A), above, these commenters stated that, without a good faith requirement for the cure, creditors and assignees could selectively cure loans only when they feared a challenge to the creditor's compliance with the ability-to-repay rule or when the creditor wanted to sell a loan on the secondary market. These commenters argued that the final rule should make clear that curing some loans selectively indicates the mortgage holder is attempting to exploit the cure in bad faith rather than making a good faith attempt to comply with the ability-to-repay rule.

#### *Final Rule*

The Bureau is finalizing § 1026.43(e)(3)(iii)(C) generally as proposed, but with changes to provide greater clarity in response to issues raised by commenters and for consistency with other provisions of this final rule. As finalized, § 1026.43(e)(3)(iii)(C) provides that, as a condition of the cure, the creditor or assignee, as applicable, must maintain and follow policies

and procedures for post-consummation review of points and fees and for making cure payments to consumers in accordance with § 1026.43(e)(3)(iii)(B) and (iv). The final commentary has been modified from the proposal to reflect and provide guidance on the final rule.

Final § 1026.43(e)(3)(iii)(C) differs from the proposal in two ways. First, the final rule requires policies and procedures “for post-consummation review of points and fees” instead of “post-consummation review of loans.” The final rule makes clear that, for purposes of exercising the cure, the required post-consummation review may focus only on points and fees and is not required to be a full loan review. Second, final § 1026.43(e)(3)(iii)(C) refers to policies and procedures for “making payments to consumers in accordance with [§ 1026.43(e)(3)(iii)(B) and (e)(3)(iv)]” rather than “refunding to consumers amounts that exceed the applicable limit under [§ 1026.43(e)(3)(i)],” for consistency with the expanded cure payment described below in the section-by-section analysis of § 1026.43(e)(iv).

To address further some of the concerns on which the comments requested clarification, comment 43(e)(3)(iii)-3 provides that the policies and procedures described in § 1026.43(e)(3)(iii)(C) need not require post-consummation review of all loans originated by the creditor or acquired by the assignee, as applicable, nor must such policies and procedures require a creditor or assignee to apply § 1026.43(e)(3)(iii) and (iv) for all loans that are found to exceed the applicable points and fees limit. The Bureau did not intend the post-consummation review requirement, as proposed, to require review of all loans, and the Bureau is making these clarifying changes to address concerns raised by commenters. As noted by industry commenters, a rule that requires review of all loans within a short time after consummation could be impracticable. Similarly, the Bureau did not intend proposed § 1026.43(e)(3)(iii)(C) to require

the creditor or assignee to make cure payments for all loans that are found to exceed the applicable points and fees limit.

The Bureau has considered commenters' concerns that the policies and procedures requirement is subjective and unnecessary or that the rule must require that the cure be exercised in good faith. The final rule includes clarifying changes to § 1026.43(e)(3)(iii)(C) and the addition of comment 43(e)(3)(iii)-3. The Bureau, however, does not believe that the requirement for policies and procedures is unnecessary or that the rule should explicitly require that the cure itself be made in good faith. Rather, the Bureau believes that the post-consummation policies and procedures requirement will serve a purpose similar to a good faith requirement while maintaining more of a "bright-line" focus, will help deter abusive practices by creditors, and will better allow regulators to monitor the use of the cure.

#### *43(e)(3)(iv)*

##### *The Bureau's Proposal*

Proposed § 1026.43(e)(3)(iii)(B) would have required the creditor or assignee to refund only the overage amount, *i.e.*, the dollar amount by which the transaction's points and fees exceeded the applicable limit under § 1026.43(e)(3)(i). The proposal solicited comment on whether other forms of cure compensation may be appropriate. For the reasons discussed below, the Bureau is adopting the cure payment provision in proposed § 1026.43(e)(3)(iii)(B) in new § 1026.43(e)(3)(iv), with modifications to require payment of interest from the time of consummation to the time of cure and to clarify that a cure payment in an amount greater than required also satisfies the cure's requirements.

##### *Comments*

Several creditors and industry trade associations stated that the cure provision should not require any cure payment beyond a refund of the overage amount. On the other hand, consumer groups generally commented that the cure provision should avoid unjustly enriching creditors or assignees and address all negative consequences to consumers such that consumers are made entirely whole.

A GSE commenter noted that requiring interest as an additional component of the cure payment would be an incentive to the creditor or assignee to detect and cure any overage as early as possible. The GSE also noted that including interest in the cure payment would come closer to making consumers whole.

Some commenters stated that creditors should be required to restructure loans if consumers financed their points and fees. Consumer group commenters expressed concern that, where consumers used loan proceeds to pay for points and fees overages, absent the overages those consumers might have borrowed smaller loan amounts with smaller monthly payments. Thus, consumer group commenters recommended that the cure provision require the creditor or assignee to apply the cure payment to the loan balance and to restructure the loan's payments and amortization schedule accordingly. Alternatively, one consumer group commenter urged a bright-line rule that would permit a cure only where the overage was not paid using loan proceeds and did not otherwise affect the terms of the loan contract.

Consumer group commenters, as well as an association of State regulators, were also concerned with overage situations where consumers paid discount points that did not reduce their interest rates as promised. In such circumstances, consumer group commenters stated that consumers should have a choice of cure compensation, including restructuring one or more loan

contract terms (*e.g.*, interest rate, payment amortization schedule), in lieu of the present value of the discount point discrepancy.

In contrast, several creditors and industry trade associations noted that a loan restructuring would be unduly complex and disruptive to the loan securitization process. A large creditor argued that a loan restructuring is unnecessary because the consumer may opt to make a prepayment with the cure payment to reduce the loan balance. That commenter further noted that the net present value of cash in the hands of the borrower may potentially outweigh future loan payments.

To clarify a potential ambiguity about whether the cure payment must be the exact amount of the overage, a GSE commenter recommended that the Bureau explicitly state that the cure provision allows the creditor or assignee to provide cure payments that are greater than the amount required by the rule. Regarding another potential ambiguity, a mortgage company commenter sought guidance as to what impacts, if any, this cure provision and the RESPA settlement charges cure provision have on one another.

#### *Final Rule*

The Bureau is adopting the cure payment provision in proposed § 1026.43(e)(3)(iii)(B) in new § 1026.43(e)(3)(iv), with modifications to require payment of interest on the points and fees overage amount from the time of consummation to the time of cure. The final rule also clarifies that a cure payment in an amount greater than required also satisfies the cure's requirements. Specifically, § 1026.43(e)(3)(iv) provides that, for purposes of § 1026.43(e)(3)(iii)(B), the creditor or assignee must make a cure payment in an amount that is not less than the sum of the following: (A) the dollar amount by which the transaction's total points and fees exceeds the applicable limit under § 1026.43(e)(3)(i); and (B) interest on the dollar amount described in

§ 1026.43(e)(3)(iv)(A), calculated using the contract interest rate applicable during the period from consummation until the cure payment is made to the consumer.

The Bureau concludes that requiring interest on the overage amount as part of the cure payment will be an incentive to creditors and assignees to detect and cure overages as early as possible and that such a requirement will go towards making consumers whole. The interest will compensate consumers for their inability to use (*e.g.*, make loan payments with) the overage funds until the time of cure. Thus, the Bureau is requiring that interest be calculated at the contract rate.

*Loan restructuring.* For purposes of this cure provision, the Bureau is not requiring loan restructuring. First, it is speculative to assume that, but for a points and fees overage, consumers might have borrowed a smaller overall loan amount. In many cases it is also possible that, without the overage, consumers would have opted to make a smaller down-payment while borrowing the same loan amount or simply would have paid less in upfront costs. Moreover, often only some of the total points and fees will be financed while some will be paid without using loan proceeds. In such situations it will be unclear whether or not an overage should be treated as having inflated the loan amount.

Second, the Bureau concludes that, even without a loan restructuring, the consumer will not be forced to pay more interest over the life of the loan. Although the Bureau recognizes that restructuring the loan payment amortization schedule would give the consumer a lower monthly interest payment, the consumer may opt to make a prepayment with the cure payment to reduce the loan balance and thereby reduce overall interest payments by paying off the loan faster. The Bureau concludes that the overall financial impact on the consumer is the same under either approach. Final comment 43(e)(3)(iii)-1 states that the cure payment may be delivered to the

consumer “by any means mutually agreeable to the consumer and the creditor or assignee,” which means that the consumer and the creditor or assignee may agree to apply the cure payment towards the loan’s unpaid principal balance (with or without reamortization) or the consumer may simply opt to make a prepayment once the cure payment is received from the creditor or assignee.

Third, a loan restructuring would be disruptive to the loan securitization process, making the cure less practicable and thus potentially harming consumers’ access to affordable credit.

*Prepayment penalties.* For purposes of this cure provision, the Bureau also is not requiring that the cure payment include any prepayment penalty associated with applying the cure payment towards the loan balance. Section 1026.32(b)(1)(v) already includes the “maximum prepayment penalty” as part of the definition of “points and fees.”<sup>22</sup> The Bureau concludes that including such amounts in the cure payment would be impractical because creditors and assignees may not know until after the cure payment is provided to the consumer whether the consumer will apply the cure payment towards the unpaid principal balance. As a practical matter, the Bureau believes that few creditors will impose such prepayment penalties, particularly since such penalties would be counted towards the points and fees limit.

*Other costs.* The final rule does not require a cure payment for other costs (beyond the points and fees overage plus interest) because the Bureau believes that such a requirement would hinder the cure provision’s intended effect of increasing access to affordable credit. The Bureau believes that attributing other costs (such as mortgage insurance premiums) to an overage is speculative and is inconsistent with the bright-line nature of qualified mortgages. The Bureau recognizes that the final rule will not make consumers entirely whole in every circumstance but

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<sup>22</sup> Section 1026.43(g)(2) limits prepayment penalties within a loan’s first two years to no more than 2 percent of the amount prepaid.

concludes that requiring and specifying how cure payments must be made for other costs would, on balance, encourage creditors to retain points and fees buffers and thus reduce access to credit.

For example, the cure provision does not require a cure payment for mortgage insurance costs paid by the consumer that arguably were increased as a result of a points and fees overage. The Bureau understands that mortgage insurance premiums are typically calculated as a percentage of the loan amount—and that percentage itself typically varies based on loan-to-value (LTV) ratios, such that some loan size increases could move a consumer from a lower-cost rate tier to a higher one. Assuming that creditors or assignees, at the time of cure, are aware of the various tiers of mortgage insurance rates in effect at consummation, the Bureau considered whether cure payments for points and fees overages should include the present value of the portion of previously-paid and future mortgage insurance payments that could be attributed to the overages (assuming that consumers would have had smaller loan amounts but for the points and fees overages).

As noted above, for purposes of the points and fees cure provision, the final rule does not assume that consumers would have had a smaller loan amount but for a points and fees overage. In many if not all cases it is uncertain whether, but for the overage, the consumer would have opted to make a smaller down-payment while borrowing the same loan amount. Moreover, in many cases only some of the total points and fees will be financed while some will be paid without using loan proceeds. In such situations it will be unclear whether an overage should be treated as having increased the loan amount.

In the final rule, the Bureau is also balancing the additional complexity of determining all potential costs that might have been caused by a points and fees overage against the expectation that most consumers will have already received pricing benefits associated with qualified

mortgages (as the creditor likely expected the loan to be a qualified mortgage). By not requiring cure payments for mortgage insurance or other costs that vary based on loan size, the cure provision will be less complicated, less risky, and otherwise less costly for creditors and assignees to use, which will encourage more easing of points and fees buffers by creditors, with attendant increases to credit access and lower credit costs for consumers.<sup>23</sup> The final rule also helps avoid disincentives for creditors to ease points and fees buffers on loans with mortgage insurance—loans that are essential for many consumers with otherwise limited access to credit.

*Discount points.* The Bureau acknowledges commenter concerns about abuses surrounding the payment of “discount points” that did not reduce the consumer’s interest rate as promised, as occurred during the period leading up to the financial crisis. Nothing in the final rule specifically addresses that practice. The Bureau believes that such a practice raises broader legal issues, including fraud and deception, which are beyond the scope of this specific cure provision. Further, the Bureau believes that payment of “discount points” that do not reduce the consumer’s interest rate as promised would raise compliance issues regardless of whether the applicable points and fees limit was exceeded. The Bureau will monitor the market for potential abuses, in particular those involving the payment of discount points that do not actually reduce the consumer’s interest rate as promised, and will consider adjustments to the rule or other actions, if appropriate.

*Relationship to RESPA tolerance cure.* Under Regulation X § 1024.7(i), if any charges at settlement exceed the charges listed on the good faith estimate of settlement costs by more than the amounts permitted under § 1024.7(e), the loan originator may cure the tolerance violation by reimbursing the amount by which the tolerance was exceeded at settlement or within 30 calendar

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<sup>23</sup> While this § 1026.43 cure provision does not require a cure payment beyond the points and fees overage plus interest, nothing in this rule should be read to limit the restitution that may be required for violations of other sections of Regulation Z or other applicable law.

days after settlement. Some settlement charges that could give rise to tolerance violations under Regulation X may also be points and fees as defined in § 1026.32(b)(1) of Regulation Z. To clarify the relationship between the Regulation X tolerance cure provision and the points and fees cure, comment 43(e)(3)(iv)-2 states that the amount paid to the consumer pursuant to § 1026.43(e)(3)(iv) may be offset by the amount paid to the consumer pursuant to 12 CFR 1024.7(i), to the extent that the amount paid to the consumer pursuant to 12 CFR 1024.7(i) is being applied to fees or charges included in points and fees pursuant to § 1026.32(b)(1). However, a creditor or assignee has not satisfied § 1026.43(e)(3)(iii) unless the total amount described in § 1026.43(e)(3)(iv), including any offset due to a payment made pursuant to 12 CFR 1024.7(i), is paid to the consumer within 210 days after consummation and prior to the occurrence of any of the events in § 1026.43(e)(3)(iii)(B)(1) through (3).<sup>24</sup>

As previously noted, the 2013 TILA-RESPA Final Rule will take effect on August 1, 2015. Among other things, the 2013 TILA-RESPA Final Rule implements in new § 1026.19(f)(2)(v) a tolerance cure provision similar to current Regulation X § 1024.7(i) that will apply, in place of Regulation X § 1024.7(i), to transactions covered by the 2013 TILA-RESPA Final Rule. Accordingly, on August 1, 2015, comment 43(e)(3)(iv)-2, described above, will be replaced by a new comment 43(e)(3)(iv)-2. That comment will provide that the amount paid to the consumer pursuant to § 1026.43(e)(3)(iv) may be offset by the amount paid to the consumer pursuant to 12 CFR 1024.7(i) or § 1026.19(f)(2)(v), to the extent that the amount paid pursuant to 12 CFR 1024.7(i) or § 1026.19(f)(2)(v) is being applied to fees or charges included in points and fees pursuant to § 1026.32(b)(1). However, a creditor or assignee has not satisfied § 1026.43(e)(3)(iii) unless the total amount described in § 1026.43(e)(3)(iv), including any offset

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<sup>24</sup> Likewise, for the Regulation X tolerance cure to be effective, it must be accomplished in accordance with the applicable Regulation X timing requirements.

due to a payment made pursuant to 12 CFR 1024.7(i) or § 1026.19(f)(2)(v), is paid to the consumer within 210 days after consummation and prior to the occurrence of any of the events in § 1026.43(e)(3)(iii)(B)(I) through (3).

## **VI. Effective Dates**

The final rule is effective on [insert date of publication in Federal Register], except that amendment 5 to Supplement I to 12 CFR Part 1026 is effective August 1, 2015 (for consistency with the 2013 TILA-RESPA Final Rule). The amendments to § 1026.43 and commentary to § 1026.43 in Supplement I to Part 1026, other than amendment 5 to Supplement I to 12 CFR Part 1026, apply to transactions consummated on or after [insert date of publication in Federal Register].

The Bureau proposed an effective date of thirty days after publication of a final rule in the **Federal Register**. The proposed changes would have expanded exemptions and provided relief from regulatory requirements; therefore the Bureau believed an effective date of 30 days after publication might be appropriate. The Bureau sought comment on whether the proposed effective date is appropriate, or whether the Bureau should adopt an alternative effective date.

One commenter representing community banks generally supported the proposed effective date. One mortgage company commenter requested clarification as to whether the rule would apply to new applications or loans consummated after the effective date. One trade association representing national mortgage lenders, servicers, and service providers recommended the proposed points and fees cure take effect immediately. Two commenters, an association of community mortgage bankers and lenders and a GSE, argued that the proposed points and fees cure should be applied to transactions consummated prior to the effective date. The GSE commenter argued that an effective date of 30 days after publication in the **Federal**

**Register** would create two classes of qualified mortgages originated during 2014: those that had the opportunity to cure and those that did not. That commenter argued that all loans consummated prior to the effective date of the new rule should be eligible for cure up to 120 days after the effective date of the rule.

As noted, the final rule (other than amendment 5 to Supplement I to 12 CFR Part 1026) is effective upon publication in the **Federal Register**. Under section 553(d) of the Administrative Procedure Act (APA), the required publication or service of a substantive rule shall be made not less than 30 days before its effective date except for certain instances, including when a substantive rule grants or recognizes an exemption or relieves a restriction. 5 U.S.C. 553(d). There are three main provisions in this final rule, each of which either expands an existing exemption or relieves a restriction. 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 expands the existing nonprofit exemption from the ability-to-repay rule by excluding certain non-interest bearing, contingent subordinate liens that meet the requirements of § 1026.43(a)(3)(v)(D) from the 200-credit extension limit calculation for purposes of qualifying for exemption. The third provision affords creditors an option, in limited circumstances, to cure mistakes in cases where a loan exceeded the applicable points and fees limit for qualified mortgages at consummation. As each of the provisions in this rule expands an existing exemption or relieves a restriction, the Bureau is publishing this final rule less than 30 days before its effective date (other than with respect to amendment 5 to Supplement I to 12 CFR Part 1026).

The Bureau considered comments requesting that loans consummated prior to the effective date be eligible for the points and fees cure, but believes that those provisions of the final rule should apply only to transactions consummated on or after the effective date (other than amendment 5 to Supplement I to 12 CFR Part 1026, which does not take effect until August 1, 2015). As discussed above, the purpose of the cure is to ensure that the Bureau's rules do not cause a restriction in access to credit while the market adjusts to the ability-to-repay and qualified mortgage rules. The Bureau understands that some creditors are refusing to make, or are making more expensive, loans with points and fees that are close to the limit for qualified mortgages, which raises concerns about access to credit. The cure is intended to encourage creditors to remove any such buffers. The Bureau believes that loans consummated after the rule takes effect could benefit from relaxed points and fees buffers. The Bureau does not, however, believe that those provisions of the rule should apply to loans consummated prior to the effective date because doing so would not further the goal of increasing access to credit.

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

### *A. Overview*

In developing the final rule, the Bureau has considered potential benefits, costs, and impacts.<sup>25</sup> 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,

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<sup>25</sup> 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.

including regarding consistency with any prudential, market, or systemic objectives administered by such agencies.

There are three main provisions in this final rule. 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 § 1026.43(a)(3)(v)(D) (“contingent subordinate liens”) from the 200-credit extension limit calculation for purposes of qualifying for the nonprofit exemption from the ability-to-repay requirements. The third provision affords creditors an option, in limited circumstances, to cure certain mistakes in cases where the loan met all of the requirements to be a qualified mortgage except that the loan actually exceeded the applicable 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 provisions against the current state of the world. That is, the Bureau’s analysis below considers the benefits, costs, and impacts of the three 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.<sup>26</sup> The baseline considers economic attributes of the relevant market and the existing regulatory structure.

The main benefit of each of these 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

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<sup>26</sup> 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.

market segments or would increase the cost of credit or servicing in those market segments in numbers sufficient to have an adverse impact on 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 provisions, all three of these scenarios would be realized, then the three 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 exemptions. However, the Bureau notes that, at least in some market segments, these three 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 either to increase the cost of credit or to curtail access to credit.

The main cost to consumers of the 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 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 financial institutions that would have complied with the ability-to-repay and mortgage servicing rules with or without the provisions may lose profits to the institutions that are able to continue operating in a market segment by virtue of one of the 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. Prior to this final rule, § 1026.41(e)(4)(ii) provided that 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 final rule adds new § 1026.41(e)(4)(ii)(C), which 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 these 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, § 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 revision of the exemption is that it creates a more level playing field for nonprofits. Prior to this final rule, for-profit affiliates could take advantage of economies of scale to service their loans together, but related nonprofits could not because they typically are not “affiliates” as defined by the BHCA.

Overall, the primary benefit to consumers of the 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 (Feb. 14, 2013). 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. Nevertheless, 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.

### *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, with negative 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 a 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-repay rule. The May 2013 ATR Final Rule exempted only nonprofit creditors that originated 200 or fewer dwelling-secured transactions 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.

Section 1026.43(a)(3)(vii) of this final rule 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-credit extension 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 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) (specifically, the “Dodd-Frank Act Section 1022(b)(2) Analysis” section in the January 2013 ATR Final Rule); 78 FR 35429, 35492-97 (June 12, 2013) (similar section 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. Nevertheless, 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, 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, with higher thresholds for loan amounts lower than \$100,000, and not including up to two bona-fide discount points. However, origination processes are not perfect, and creditors might be concerned about potential errors that result in a loan exceeding the applicable points and fees limit discovered upon further, post-consummation review.

The three most likely responses by a creditor concerned about such errors would be to originate loans with points and fees well below the applicable limit, to insert additional quality control in its origination process, and 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 the applicable limit. Such creditors might adopt any one, or any combination of two or more, of these responses. 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 economically efficient amount of effort expended on quality control. 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 the applicable points and fees 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 and undesirable consequence of the rule.

The final rule provides a limited post-consummation cure provision that creditors or assignees may exercise when they discover errors in points and fees calculations that resulted in loans exceeding the applicable points and fees limit. The primary potential drawback of allowing creditors and assignees to cure such errors is the risk of inappropriate exploitation. However, the conditions the Bureau has placed on the cure mechanism—such as limiting the cure period to 210 days after consummation and cutting off the creditor's and assignee's ability to cure when the consumer files an action in connection with the loan or provides written notice of the overage to the creditor, assignee, or servicer, or when the consumer becomes 60 days past

due on the legal obligation—help to guard against abuse of this mechanism and thus ensure that consumers are unlikely to experience negative side-effects.

One such potential exploitation 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 and effects a cure of the points and fees overage before the consumer becomes 60 days past due on the legal obligation, files a lawsuit, or provides written notice of the points and fees overage. The elements of § 1026.43(e)(3)(iii) requiring that the overage be cured within 210 days after consummation and before certain cut-off events should discourage this type of exploitation. Another exploitation scenario is a creditor that only cures overages on loans that go into foreclosure; however, this possibility is limited by the past-due cut-off and the 210-day cure window.

The Bureau proposed a requirement that, to cure a points and fees overage, the loan must have been originated in good faith as a qualified mortgage. The Bureau is not adopting this requirement in the final rule. The Bureau also proposed a 120-day cure period, and it is finalizing a 210-day cure period instead. While both of these requirements would have provided additional protections against inappropriate exploitation by creditors, the Bureau believes that these two requirements would be sufficiently burdensome for creditors that significantly fewer creditors would utilize the cure provision. The Bureau believes the 210-day window, combined with the creditors being able to exercise the cure only before the occurrence of certain cut-off events, provides sufficient disincentives against inappropriate exploitation.

The primary benefit to consumers of the 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 a points and fees overage, the creditor may reimburse the consumer for the overage and interest on the overage from the time of consummation until the cure is effectuated. However, this is a benefit only for consumers who place greater value on being reimbursed than on preserving a potential ability-to-repay claim. 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 qualified mortgage presumption of TILA ability-to-repay compliance. However, the Bureau believes that the safeguards included in the rule will mitigate this potential concern as creditors are unlikely to be able to exploit the rule inappropriately 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.

The Bureau believes that the benefits of this provision are likely to decrease over time, as creditors familiarize themselves with points and fees calculations necessary for origination of qualified mortgages and institute even better and more efficient quality control processes. All creditors could then originate loans with points and fees close to or at the applicable limit, without charging either an extra risk premium or having to incur significant quality control costs.

However, some exploitation incentives and costs to consumers may remain. Therefore, the Bureau is finalizing the cure provision with a sunset date of January 10, 2021.

Finally, the Bureau does not possess any data that would enable it to report the number of transactions affected. For some creditors, the provision might save additional verification and quality control in the loan origination process for every qualified mortgage transaction that they originate<sup>27</sup> and/or allow them to originate loans with points and fees close to or at the applicable points and fees limit at lower prices that do not reflect the risk of the loan unexpectedly turning out not to be a qualified mortgage.

Several consumer groups commented that there is no evidence to support the assertion that the points and fees cure provision adopted by this final rule will provide consumer benefits. As noted above, the Bureau does not possess any data to calculate the impact of this provision on consumer welfare, the likely costs of credit, or the availability of access to credit. No commenters suggested data sources.

The Bureau is aware that after the comment period closed some data became available, as the Federal Reserve System released its July 2014 installment of the Senior Loan Officer Opinion Survey.<sup>28</sup> Several questions (for example, survey question 18e) were regarding the points and fees qualified mortgage limit, and whether it affected certain aspects of creditors' practices. Most of the responses indicated that the points and fees limits did not have a significant effect. Given that this is not a representative survey and that the survey has qualitative replies, the Bureau still does not have sufficient data to calculate the effect of this

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<sup>27</sup> While a result of the 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 on which to focus. In addition, the incentive to limit (to an undesirable extent) pre-consummation quality control measures is mitigated by the fact that effecting the cure is not without costs, both operational and reputational.

<sup>28</sup> Bd. of Governors of the Fed. Reserve Sys., *July 2014 Senior Loan Officer Opinion Survey on Bank Lending Practices*, (August 4, 2014), available at <http://www.federalreserve.gov/boarddocs/snloansurvey/201408/fullreport.pdf>.

provision on consumer welfare, the likely costs of credit, or the availability of access to credit.

Moreover, as mentioned in part VII.C, the Bureau believes that this provision will largely benefit smaller creditors (and, potentially, their consumers), whereas larger creditors are sampled at a higher rate than smaller creditors in the Senior Loan Officer Opinion Survey.

*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 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 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 provision might not benefit them as much. The third provision may lead smaller creditors to extend a greater number of qualified mortgages near or at the applicable 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 the origination of loans with points and fees close to or at the applicable limit for qualified mortgages—might negatively affect access to credit in those areas 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.

The final rule will not have a significant economic impact on any small entities. As noted in the Section 1022(b)(2) Analysis, above, the Bureau does not expect the rule to impose costs on covered persons, including small entities. All methods of compliance under current law will remain available to small entities when these provisions become effective. Thus, a small entity that is in compliance with current law need not take any additional action if the proposal is

adopted. Further, the Bureau does not possess any data that would enable it to report the number of transactions affected, including transactions involving small entities.

Accordingly, the undersigned certifies that this rule will 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 final 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.

## **List of Subjects**

### **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 amends 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 paragraph (e)(4)(ii) and the introductory text of paragraph (e)(4)(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 satisfies 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 satisfies 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)(I) and adding new paragraph (a)(3)(vii) and by revising the introductory text of paragraph (e)(3)(i) and adding new paragraphs (e)(3)(iii) and (e)(3)(iv) to read as follows:

**§ 1026.43 Minimum standards for transactions secured by a dwelling.**

(a) \* \* \*

(3) \* \* \*

(v) \* \* \*

(D) \* \* \*

(I) 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)(I) of this section:

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

(B) The transaction is for the purpose of:

(I) 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:

(I) 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) \* \* \* (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) For covered transactions consummated on or before January 10, 2021, if the creditor or assignee determines after consummation that the transaction's total points and fees 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 loan otherwise meets the requirements of paragraphs (e)(2), (e)(4), (e)(5), (e)(6), or (f) of this section, as applicable;

(B) The creditor or assignee pays to the consumer the amount described in paragraph (e)(3)(iv) of this section within 210 days after consummation and prior to the occurrence of any of the following events:

(1) The institution of any action by the consumer in connection with the loan;

(2) The receipt by the creditor, assignee, or servicer of written notice from the consumer that the transaction's total points and fees exceed the applicable limit under paragraph (e)(3)(i) of this section; or

(3) The consumer becoming 60 days past due on the legal obligation; and

(C) The creditor or assignee, as applicable, maintains and follows policies and procedures for post-consummation review of points and fees and for making payments to consumers in accordance with paragraphs (e)(3)(iii)(B) and (e)(3)(iv) of this section.

(iv) For purposes of paragraph (e)(3)(iii) of this section, the creditor or assignee must pay to the consumer an amount that is not less than the sum of the following:

(A) The dollar amount by which the transaction's total points and fees exceeds the applicable limit under paragraph (e)(3)(i) of this section; and

(B) Interest on the dollar amount described in paragraph (e)(3)(iv)(A) of this section, calculated using the contract interest rate applicable during the period from consummation until the payment described in this paragraph (e)(3)(iv) is made to the consumer.

\* \* \* \*

4. In Supplement I to part 1026:

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

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

- ii. Under *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, 2, and 3 under that subheading are added.
  - iii. Effective [insert date of publication in Federal Register] new subheading *Paragraph 43(e)(3)(iv)* 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 under § 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 the 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 the 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 the 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 the 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) in applying § 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 pursuant to § 1026.41(e)(4)(iii)(A). 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 satisfies § 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) in applying § 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 satisfies § 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)(I), 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. Payment to the consumer.* The creditor or assignee, as applicable, complies with § 1026.43(e)(3)(iii)(B) if it pays to the consumer the amount described in § 1026.43(e)(3)(iv) within 210 days after consummation and prior to the occurrence of any of the events in § 1026.43(e)(3)(iii)(B)(1) through (3). A creditor or assignee, as applicable, does not comply with § 1026.43(e)(3)(iii)(B) if it pays to the consumer the amount described in § 1026.43(e)(3)(iv) more than 210 days after consummation or after the occurrence of any of the events in § 1026.43(e)(3)(iii)(B)(1) through (3). Payment may be made by any means mutually agreeable to the consumer and the creditor or assignee, as applicable, or by check. If payment is made by check, the creditor or assignee complies with § 1026.43(e)(3)(iii)(B) if the check is delivered or placed in the mail to the consumer within 210 days after consummation.

*2. 60 days past due.* Section 1026.43(e)(3)(iii)(B)(3) provides that, to comply with § 1026.43(e)(3)(iii)(B), the creditor or assignee must pay to the consumer the amount described in § 1026.43(e)(3)(iv) prior to the consumer becoming 60 days past due on the legal obligation. For this purpose, “past due” means the failure to make a periodic payment (in one full payment or in two or more partial payments) sufficient to cover principal, interest, and, if applicable,

escrow under the terms of the legal obligation. Other amounts, such as any late fees, are not considered for this purpose. For purposes of § 1026.43(e)(3)(iii)(B)(3), a periodic payment is 30 days past due when it is not paid on or before the due date of the following scheduled periodic payment and is 60 days past due when, after already becoming 30 days past due, it is not paid on or before the due date of the next scheduled periodic payment. For purposes of § 1026.43(e)(3)(iii)(B)(3), the creditor or assignee may treat a received payment as applying to the oldest outstanding periodic payment. The following example illustrates the meaning of 60 days past due for purposes of § 1026.43(e)(3)(iii)(B)(3):

i. Assume a loan is consummated on October 15, 2015, that the consumer's periodic payment is due on the 1st of each month, and that the consumer timely made the first periodic payment due on December 1, 2015. For purposes of § 1026.43(e)(3)(iii)(B)(3), the consumer is 30 days past due if the consumer fails to make a payment (sufficient to cover the scheduled January 1, 2016 periodic payment of principal, interest, and, if applicable, escrow) on or before February 1, 2016. For purposes of § 1026.43(e)(3)(iii)(B)(3), the consumer is 60 days past due if the consumer then also fails to make a payment (sufficient to cover the scheduled January 1, 2016 periodic payment of principal, interest, and, if applicable, escrow) on or before March 1, 2016. For purposes of § 1026.43(e)(3)(iii)(B)(3), the consumer is not 60 days past due if the consumer makes a payment (sufficient to cover the scheduled January 1, 2016 periodic payment of principal, interest, and, if applicable, escrow) on or before March 1, 2016.

*3. Post-consummation policies and procedures.* The policies and procedures described in § 1026.43(e)(3)(iii)(C) need not require that a creditor or assignee, as applicable, conduct a post-consummation review of all loans originated by the creditor or acquired by the assignee, nor must such policies and procedures require a creditor or assignee to apply § 1026.43(e)(3)(iii) and

(iv) for all loans for which the total points and fees are found to exceed the applicable limit under § 1026.43(e)(3)(i).

*Paragraph 43(e)(3)(iv).*

*1. Interest rate.* For purposes of § 1026.43(e)(3)(iv)(B), interest is calculated using the contract interest rate applicable during the period from consummation until the payment described in § 1026.43(e)(3)(iv) is made to the consumer. In an adjustable-rate or step-rate transaction in which more than one interest rate applies during the period from consummation until payment is made to the consumer, the minimum payment amount is determined by calculating interest on the dollar amount described in § 1026.43(e)(3)(iv)(A) at each such interest rate for the part of the overall period during which that rate applies. However, § 1026.43(e)(3)(iv) provides that, for purposes of § 1026.43(e)(3)(iii), the creditor or assignee can pay to the consumer an amount that exceeds the sum of the amounts described in § 1026.43(e)(3)(iv)(A) and (B). Therefore, a creditor or assignee may, for example, elect to calculate interest using the maximum interest rate that may apply during the period from consummation until payment is made to the consumer. See comment 43(e)(3)(iii)-1 for guidance on making payments to the consumer.

*2. Relationship to RESPA tolerance cure.* Under Regulation X (12 CFR 1024.7(i)), if any charges at settlement exceed the charges listed on the good faith estimate of settlement costs by more than the amounts permitted under 12 CFR 1024.7(e), the loan originator may cure the tolerance violation by reimbursing the amount by which the tolerance was exceeded at settlement or within 30 calendar days after settlement. The amount paid to the consumer pursuant to § 1026.43(e)(3)(iv) may be offset by the amount paid to the consumer pursuant to 12 CFR 1024.7(i), to the extent that the amount paid to the consumer pursuant to 12 CFR 1024.7(i) is

being applied to fees or charges included in points and fees pursuant to § 1026.32(b)(1). However, a creditor or assignee has not satisfied § 1026.43(e)(3)(iii) unless the total amount described in § 1026.43(e)(3)(iv), including any offset due to a payment made pursuant to 12 CFR 1024.7(i), is paid to the consumer within 210 days after consummation and prior to the occurrence of any of the events in § 1026.43(e)(3)(iii)(B)(1) through (3).

\* \* \* \*

5. Effective August 1, 2015, in Supplement I to Part 1026, under Section 1026.43, subheading *Paragraph 43(e)(3)(iv)* and paragraph 2 under that subheading is amended.

The revisions read as follows:

*Section 1026.43—Minimum Standards for Transactions Secured by a Dwelling*

\* \* \* \*

*Paragraph 43(e)(3)(iv).*

\* \* \* \*

2. *Relationship to RESPA tolerance cure.* Under Regulation X (12 CFR 1024.7(i)), if any charges at settlement exceed the charges listed on the good faith estimate of settlement costs by more than the amounts permitted under 12 CFR 1024.7(e), the loan originator may cure the tolerance violation by reimbursing the amount by which the tolerance was exceeded at settlement or within 30 calendar days after settlement. Similarly, under § 1026.19(f)(2)(v), if amounts paid by the consumer exceed the amounts specified under § 1026.19(e)(3)(i) or (ii), the creditor complies with § 1026.19(e)(1)(i) if the creditor refunds the excess to the consumer no later than 60 days after consummation. The amount paid to the consumer pursuant to § 1026.43(e)(3)(iv) may be offset by the amount paid to the consumer pursuant to 12 CFR 1024.7(i) or § 1026.19(f)(2)(v), to the extent that the amount paid to the consumer pursuant to 12 CFR

1024.7(i) or § 1026.19(f)(2)(v) is being applied to fees or charges included in points and fees pursuant to § 1026.32(b)(1). However, a creditor or assignee has not satisfied § 1026.43(e)(3)(iii) unless the total amount described in § 1026.43(e)(3)(iv), including any offset due to a payment made pursuant to 12 CFR 1024.7(i) or § 1026.19(f)(2)(v), is paid to the consumer within 210 days after consummation and prior to the occurrence of any of the events in § 1026.43(e)(3)(iii)(B)(1) through (3).

\* \* \* \*

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

Dated: October 17, 2014.



**Richard Cordray,**

*Director, Bureau of Consumer Financial Protection.*