

ICBA Summary of the High-Cost Mortgage / Home Ownership and Equity Protection (HOEPA) Rule

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I. BACKGROUND

The Home Ownership and Equity Protection Act (HOEPA) was enacted in 1994 as an amendment to the Truth in Lending Act (TILA) to address abusive practices in refinances and closed-end home equity loans with high interest rates or high fees. In 2010, the Dodd-Frank Act amended TILA by expanding the scope of HOEPA coverage to include purchase-money mortgages and open-end credit plans (i.e., home equity lines of credit, or HELOCs) and amended HOEPA's coverage tests.

In January 2013, the Consumer Financial Protection Bureau (CFPB) issued the 2013 HOEPA rule that amended TILA's Regulation Z to implement the Dodd-Frank Act's changes to HOEPA. The 2013 HOEPA Rule also implemented two additional Dodd-Frank counseling requirements that may apply to creditors regardless of whether or not they make high-cost mortgages. Specifically, these provisions require or encourage consumers to obtain homeownership counseling for other types of loans. The rule is effective for applications received on or after January 10, 2014.

Applicability to Community Banks

The High-Cost Mortgage/HOEPA Rule applies to community banks. However, community banks that are small creditors (less than \$2 billion in assets (as adjusted annually) and originating fewer than 2,000 loans per year, excluding portfolio loans) that extended a covered transaction secured by a first-lien on a property located in a rural or underserved area in the previous calendar year, or for applications received before April 1 of a calendar year in either of the two prior calendar years, can rely on the exemption to the general prohibition on balloon loans subject to certain conditions of the Ability to Repay / Qualified Mortgage rule.

Link to the CFPB's HOEPA Rule Resource Page - <http://www.consumerfinance.gov/regulations/high-cost-mortgage-and-homeownership-counseling-amendments-to-regulation-z-and-homeownership-counseling-amendments-to-regulation-x/>

II. SCOPE

Under the 2013 HOEPA rule, most types of mortgage loans secured by a consumer's principal dwelling¹, including purchase money mortgages, refinances, closed-end home-equity loans, and open-end credit plans (i.e., home equity lines of credit (HELOCs)), are potentially subject to HOEPA coverage.

¹ Mortgages secured by manufactured housing (whether titled as real property or personal property) and other types of personal property (e.g., an RV or a houseboat) are subject to HOEPA coverage if the dwelling is the consumer's principal dwelling.

These loans are exempt from the HOEPA requirements:

- Reverse mortgages;
- Loans to finance the initial construction of a dwelling²;
- Loans directly financed by Housing Finance Agencies; and
- Loans directly financed through the Rural Housing Service section 502 Direct Loan Program.

III. HOEPA Coverage Test

If a loan falls under the scope of the rule it is considered a HOEPA loan if:

- The transaction's annual percentage rate (APR) exceeds the applicable average prime offer rate (APOR) for mortgage transactions, which is published on the FFIEC website, by more than 6.5 percentage points for first lien mortgages, or by more than 8.5 percentage points for a first mortgage if the dwelling is personal property and the transaction is for less than \$50,000;
- The transaction's APR exceeds the applicable APOR by more than 8.5 percentage points for subordinate or junior mortgages;
- The transaction's points and fees exceed 5 percent of the total transaction amount for loan amounts greater than \$20,000³; and for loans below \$20,000, the lesser of 8 percent of the total transaction amount or \$1,000⁴ (with dollar figures adjusted annually for inflation); OR
- The credit transaction documents permit the creditor to charge or collect a prepayment penalty more than 36 months after transaction closing or permit such fees or penalties to exceed, in the aggregate, more than 2 percent of the amount prepaid.

IV. Restrictions on Loan Terms for High-Cost Mortgages

The final rule also includes restrictions and requirements concerning loan terms and origination practices for high-cost mortgages/HOEPA loans. For example:

- Balloon payments are generally banned, unless they are to account for the seasonal or irregular income of the borrower, they are part of a short-term bridge loan (12 months or less), or they are made by small creditors (less than \$2 billion in assets⁵ and originating fewer than 2,000 loans per year, excluding portfolio loans) that extended a covered transaction secured by a first-lien on a property located in a rural or underserved area in the previous calendar year, or for applications received before April 1 of a calendar year in either of the two prior calendar years, and meet certain criteria.
- Creditors are prohibited from charging prepayment penalties.

² When a construction-to-permanent loan is made as two separate transactions, the construction loan transaction is exempt from the HOEPA requirements, but the permanent financing transaction is not. For a construction-to-permanent loan originated as a single transaction, coverage must be determined in accordance with appendix D to Regulation Z.

³ Effective January 1, 2017, this threshold will increase to \$20,579.

⁴ Effective January 1, 2017, this threshold will increase to \$1,029.

⁵ For 2017 this threshold is set at \$2.069 billion.

- Late fees are restricted to four percent of the payment that is past due, fees for providing payoff statements are restricted, and fees for loan modification or payment deferral are banned.
- Creditors originating HELOCs are required to assess the consumer's ability to repay as of account opening, including assessment of consumer's current and reasonably expected income, employment, assets other than the collateral, current obligations, and property tax and insurance obligations. A creditor may base its determination of repayment ability on current or reasonably expected income from employment or other sources, on assets other than the collateral, or both.
- Creditors and mortgage brokers are prohibited from recommending or encouraging a consumer to default on a loan or debt to be refinanced by a high-cost mortgage.
- Before making a high-cost mortgage, creditors are required to obtain confirmation from a federally certified or approved homeownership counselor that the consumer has received counseling on the advisability of the mortgage.
- Due-on-demand features that allow for acceleration in high-cost mortgages are allowed only in cases where:
 - The consumer commits fraud or makes a material misrepresentation in connection with the loan or credit agreement.
 - The consumer defaults on payment.
 - The consumer's action or inaction adversely affects the creditor's security interest for the loan.

V. Additional Restrictions

- Fees for generation of payoff statements are generally banned, with limited exceptions.
- Points and fees cannot be financed (i.e., rolled into the loan amount). However, you can finance closing charges excluded from the definition of points and fees, such as bona fide third-party charges.
- A creditor cannot purposely structure a transaction to evade HOEPA coverage (for example, splitting a loan into two loans to divide the loan fees to avoid the points-and-fees threshold).
- Negative amortization is prohibited in a high-cost mortgage.
- A payment schedule that consolidates more than two periodic payments and pays them in advance from loan proceeds is prohibited in a high-cost mortgage.
- An increase in the interest rate after default is prohibited in a high-cost mortgage.
- In the case of acceleration as a result of default in payment, a refund of interest calculated in a manner less favorable to the consumer than the actuarial method is prohibited in a high-cost mortgage.
- Paying a contractor under a home-improvement contract from the proceeds of a high-cost mortgage is prohibited (with certain exceptions).
- Selling a high-cost mortgage in the secondary market without providing a high-cost mortgage notice to the assignee is prohibited.
- Refinancing any high-cost mortgage into another high-cost mortgage within one year after having extended credit is prohibited, unless the refinancing is in the consumer's interest.

VI. Ability to Repay Requirements

The rule requires you to determine a consumer's ability to repay a high-cost mortgage prior to consummation or account opening. There are different rules for closed-end high-cost mortgages and open-end high-cost mortgages (HELOCs). The Dodd-Frank Act established new ability-to-repay requirements for most closed-end mortgage loans, including high-cost mortgages. These requirements were implemented in the Bureau's Ability-to-Repay (ATR) /Qualified Mortgage (QM) rule.

The QM/ATR requirements do not apply to HELOCs. Thus, for open-end high-cost mortgages, repayment ability will still be determined using HOEPA's ATR rules. In general, a creditor must consider the consumer's:

- Current and reasonably expected income or assets (verified with W-2s, tax returns, payroll receipts, financial institution records, or other third-party documents that provide reasonably reliable evidence).
- Current obligations, including any mortgage-related obligations such as property taxes, required insurance premiums, community association fees, ground rent, and leasehold payments. These repayment-ability provisions still provide for a presumption of compliance if specified criteria are met

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VII. Counseling Requirements

Creditors must provide a list of homeownership counseling organizations to most mortgage loan applicants within three days of application. This requirement applies to most types of closed-end and open-end credit transactions, including high-cost mortgages.

Prior to making a high-cost mortgage, a creditor must receive written certification that the consumer has received homeownership counseling on the advisability of the mortgage from a HUD approved counselor or a state housing finance authority, if permitted by HUD. The homeownership counselor cannot be affiliated with or employed by the creditor and the creditor cannot steer the consumer to a particular counseling agency.

The required counseling must cover the following topics:

1. Key terms of the mortgage transaction as set out in the relevant disclosure;
2. The consumer's budget, including the consumer's income, assets, financial obligations, and expenses; and
3. The affordability of the mortgage transaction for the consumer.

The consumer must have received either the Loan Estimate required under the TILA RESPA integrated Disclosure rule or the disclosures required for HELOCs before the homeownership counseling session on the advisability of the mortgage. For transactions where neither the Loan Estimate nor the § 1026.40 disclosure for HELOCs is provided, counseling must occur after the consumer receives the disclosures required for high-cost mortgages.

The rule does not require in-person counseling. Counseling may be provided via telephone, so long as it is provided by a HUD-approved counselor. A self-study program may not be used to satisfy the counseling requirement.

VIII. HOEPA Required Disclosures

A creditor must provide a disclosure to consumers at least three business days prior to consummation or account opening of a high-cost mortgage. The disclosure must be in writing and in a form the consumer may keep, and must:

- Inform the consumer that the loan will not be effective until consummation or account opening occurs;
- Explain the consequences of default;
- Disclose loan terms such as APR, amount borrowed, and monthly payment; and
- In the case of variable-rate loans, explain the maximum monthly payment that may be required under the terms of the loan or credit plan