

**2008 Amendments to regulation Z  
(Truth in Lending & Home Ownership and Equity Protection)  
And  
2008 CONFORMING AMENDMENTS TO REGULATION C  
(HOME MORTGAGE DISCLOSURE)**

**REGULATION Z: Enhanced Consumer Protections for Closed-End Mortgage Loans**

The closed-end mortgage provisions of Regulation Z, implementing the Truth in Lending and Home Ownership and Equity Protection Acts, have been amended. The amended provisions now include consumer protections specific to "higher-priced mortgage loans," revised prepayment penalty provisions for high-cost (Regulation Z Section 32) mortgage loans, prohibitions relating to servicing, appraisers, and advertising, and expanded early disclosure requirements.<sup>1</sup>

**Prohibited Practices for "Higher-Priced Mortgage Loans"**

The rule creates a new category of mortgage loans. A "higher-priced mortgage loan" is any mortgage (purchase-money or non-purchase-money) secured by a consumer's principal dwelling with an Annual Percentage Rate (APR) exceeding the "average prime offer rate" on prime loans (published by the Federal Reserve Board (FRB)) by at least 1.50 percentage points for first-lien loans and 3.50 percentage points for subordinate-lien loans.

The "average prime offer rate" is an APR derived from average interest rates, points, and other loan pricing terms offered to consumers by a representative sample of creditors for mortgage transactions with low-risk pricing characteristics.

Creditors originating higher-priced mortgage loans are prohibited from:

- Relying on the collateral securing the loan without regard to the consumer's ability to repay the loan;
- Relying on the consumer's income or assets without verifying such amounts through reasonably reliable third-party documents; **and**
- Imposing a prepayment penalty if the consumer's payment can change in the first 4 years of the loan term. (*Otherwise, a creditor is permitted to impose a penalty for prepayment but only within the first 2 years of the term.*)

Creditors are also prohibited from originating a higher-priced mortgage loan **secured by a first lien** without establishing an escrow account for property taxes and homeowners' insurance. A creditor is permitted to offer the borrower the opportunity to cancel the escrow 12 months after consummation.

**Revisions to High-Cost Mortgage (Regulation Z Section 32) Provisions**

- The rule extends the higher-priced mortgage loan protections to mortgage loans covered by Section 32 of Regulation Z ("high-cost mortgage loans").<sup>2</sup>

<sup>1</sup> See *Federal Register* Vol. 73, No.147, July 30, 2008, page 44522. <http://edocket.access.gpo.gov/2008/pdf/E8-16500.pdf> 565K (PDF Help)

<sup>2</sup> 12 C.F.R. § 226.32, <http://www.fdic.gov/regulations/laws/rules/6500-1800.html#6500226.32>. Unlike "higher-priced" mortgage loans, Section 32 "high-cost" mortgage loans are limited to non-purchase money home loans (i.e., mortgage loans on homes already owned, such as refinancings or home equity

- The rule revises the prepayment penalty provisions for high-cost (Section 32) mortgage loans as follows:
  - limits prepayment penalty period to first 2 years (reduced from five years under the former rule);
  - prohibits prepayment penalty, without exception, if periodic payment (e.g., monthly payment) can change in first four years.

### **Prohibited Practices for All Closed-End Mortgage Loans Secured by a Consumer's Principal Dwelling**

For all closed-end mortgage loans secured by a consumer's principal dwelling (not limited to higher-priced mortgage loans), the rule prohibits:

1. **Creditors and mortgage brokers** from coercing, influencing, or encouraging an appraiser to misrepresent the value of the property.<sup>3</sup>(The rule also prohibits creditors from extending credit when a creditor knows that a person has coerced, influenced, or encouraged an appraiser, unless the creditor acts with reasonable diligence to determine that the appraisal does not materially misstate or misrepresent the value of the property.)
2. **Servicers** from failing to credit a payment to the consumer's account as of the date of its receipt; failing to provide a pay-off statement within a reasonable amount of time after a request; and "pyramiding" late fees (i.e., levying or collecting a delinquency charge on a payment, when the only delinquency is attributable to late fees or delinquency charges assessed on earlier installments).

### **Prohibited Practices for All Closed-End Mortgage Loans Secured by a Dwelling**

loans). Consumers of high cost mortgage loans receive special protections including prohibition of: balloon payments on mortgages with a term of less than five years, negative amortization, and default penalty rates. For a mortgage loan to be "high cost," its APR must exceed by more than eight percentage points for first-lien loans, or by more than ten percentage points for subordinate-lien loans, the yield on Treasury securities having comparable periods of maturity to the loan maturity as of the fifteenth day of the month immediately preceding the month in which the mortgage loan application is received by the creditor. *(Alternatively, a mortgage is a high-cost mortgage where the total points and fees payable by the consumer at or before closing will exceed the greater of eight percent of the total loan amount, or – as of the date of this FIL - \$561. Effective January 1, 2009, the minimum threshold for total fees and points will increase from \$561 to \$583.)*

As noted, for a mortgage loan to be "higher-priced," its APR must exceed the "average prime offer rate" by at least 1.50 percentage points for first-lien loans and 3.50 percentage points for subordinate-lien loans. As such, Section 32 high cost mortgage loans represent a subset of Regulation Z's "higher-priced" mortgage loans. Thus, consumers of high-cost mortgages receive protections applicable to both high-cost **and** higher-priced mortgages.

<sup>3</sup> Though Regulation Z limits the coverage of this prohibition to mortgage loans secured by a consumer's principal dwelling, depending on the facts and circumstances, the FDIC may take action against such practices relative to **any** mortgage loan under the standards for unfair or deceptive acts or practices pursuant to Section 5 the Federal Trade Commission Act. Also, the FDIC has promulgated regulations and guidance that set forth standards for the policies and procedures FDIC-supervised institutions are expected to implement to ensure the independent judgment of appraisers when valuing property. See Appraisals at 12 CFR 323, <http://www.fdic.gov/regulations/laws/rules/2000-4300.html> and Real Estate Lending Standards at 12 CFR 365, <http://www.fdic.gov/regulations/laws/rules/2000-8700.html> .

For closed-end mortgage loans secured by a dwelling, the rule identifies and prohibits several misleading or deceptive advertising practices, including representations that a rate or payment is "fixed" when it can change. The rule requires that advertisements provide accurate and balanced information, in a clear and conspicuous manner, about rates, monthly payments, and other loan features. Specifically, the rule requires that advertisements state all applicable rates or payments with equal prominence and in close proximity to any advertised promotional or "teaser" rate or payment.

### **Extension of Early Disclosure Requirements to Non-Purchase-Money Mortgages**

The rule extends the current early disclosure requirement for purchase-money mortgage transactions to transactions involving refinancings and home equity loans secured by the consumer's principal dwelling. In addition, except to the extent such fee is for the purpose of obtaining a credit report, the rule prohibits creditors from assessing an application fee for a closed-end mortgage transaction until after a consumer has received the early disclosures.

### **REGULATION C: Revised Loan Data Compilation and Reporting Requirements**

The compilation and reporting of loan data provisions of Regulation C, implementing the Home Mortgage Disclosure Act, have been amended to conform to Regulation Z's definition of higher-priced mortgage loans.<sup>4</sup> Since 2004, Regulation C has required lenders to collect and report the spread between the APR on a loan and the yield on Treasury securities of comparable maturity if the spread is equal to or greater than 3.0 percentage points for a first-lien loan (or 5.0 percentage points for a subordinate-lien loan).

Under the amended provisions, a lender will report the spread between the loan's APR and a survey-based estimate of APRs (to be updated weekly by the FRB) currently offered on prime mortgage loans of a comparable type (the "average prime offer rate") if the spread is equal to or greater than 1.5 percentage points for a first-lien loan (or 3.5 percentage points for a subordinate-lien loan). The FRB will rely on the "Primary Mortgage Market Survey" conducted by Freddie Mac to establish the average prime offer rate.

**Effective Date: October 1, 2009** for all provisions except those relating to Regulation Z's escrowing for higher-priced mortgage loans. For escrow provisions: April 1, 2010 (October 1, 2010 for the escrow provisions applicable to manufactured housing).

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<sup>4</sup> See *Federal Register* Vol. 73, No.207, October 24, 2008, page 63329. <http://edocket.access.gpo.gov/2008/pdf/E8-25320.pdf> (PDF Help)