ICBA Summary of the Final Rule Expanding the "Small Creditor" & "Rural" Definitions in the Regulation Z Mortgage Rules

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Final Rule Expanding the "Small Creditor" and "Rural" Definitions in the Regulation Z Mortgage Rules

I. BACKGROUND

On September 21, 2015, the Consumer Financial Protection Bureau (CFPB) issued a final rule amending certain ability-to-repay (ATR)/qualified mortgage (QM) rules and escrow requirements in Regulation Z (Truth in Lending Act) issued in 2013. The rule revises the CFPB's regulatory definitions of "small creditor" and "rural" areas, for purposes of certain special provisions and exemptions from various requirements provided to small creditors. The proposed amendments were issued in January 2015 and the final rule makes no significant changes to the original proposal.

Link to the CFPB summary and final rule - http://www.consumerfinance.gov/newsroom/cfpb-issues-proposal-to-facilitate-access-to-credit-in-rural-and-underserved-areas/

II. Provisions of the Final Rule

The final rule amends the current ATR/QM provisions and escrow requirements for higher-priced mortgage loans (HPML) by:

- **Expanding the definition of "small creditor":** The loan origination limit for determining eligibility for small-creditor status (based on the preceding calendar year's originations of the creditor and its affiliates) is increased from 500 originations of covered transactions secured by a first lien, to 2,000 such originations, and excludes originated loans held in portfolio by the creditor and its affiliates from that limit. So, lenders otherwise meeting the small creditor requirements could originate an unlimited amount of portfolio loans which would have small creditor QM status.[1]

[1] Currently, a loan is considered a "small creditor" QM loan if:

- It is originated and held in portfolio for at least 3 years;
- It is originated by a *"small creditor,"* which is a creditor with under $2.060 billion in assets and under 500 first lien mortgage loans originated in a calendar year;
- It meets the general restrictions on qualified mortgages with regard to loan features and points and fees; **AND**
- Creditors evaluate consumers' debt-to-income (DTI) ratio or residual income.

For creditors that satisfy this exception:

- QM first-lien loans receive safe harbor protection if they are less than 3.5 percentage points above the average prime offer rate (APOR) and
- The loans **are not** subject to the 43 percent DTI ratio as they would be under the general qualified mortgage definition.

The final rule also creates a grace period from calendar year to calendar year to allow a creditor that exceeds the origination limit in the preceding calendar year to operate, in certain circumstances, as a small creditor with respect to applications received prior to April 1 of the current calendar year.

- **Including mortgage affiliates in the calculation of small-creditor status:** The final rule does not change the current asset limit for small-creditor status, which is set at less than $2.060 billion (adjusted annually) in total assets as of the end of the preceding calendar year. However, it does include the assets of the creditor's mortgage-originating affiliates in calculating whether a creditor is under the limit. The CFPB has also added a grace period to the annual asset limit, similar to the grace period added to the origination limit, to allow a creditor that exceeded that threshold in the preceding calendar year to operate, in certain circumstances, as a small creditor with respect to applications received before April 1 of the current calendar year.

- **Expanding the definition of "rural" areas:** In addition to counties that are considered to be "rural" under the CFPB's current mortgage rules, the final rule expands the definition of "rural" by including all census blocks that are not in an urban area as defined by the U.S. Census Bureau (Census Bureau).[2] This will allow more community bank balloon mortgage loans to receive QM safe harbor legal status and would allow more community banks to be exempt from escrow requirements for HPMLs.

- **Providing grace periods for small creditor and rural or underserved creditor status:** Creditors that exceed the origination limit or asset-size limit in the preceding calendar year will be allowed to operate, in certain circumstances, as a small creditor with respect to mortgage transactions with applications received prior to April 1 of the current calendar year. The final rule also creates a similar grace period for creditors that no longer operated predominantly in rural or underserved areas during the preceding calendar year.

- **Creating a one-year qualifying period for rural or underserved creditor status:** The final rule adjusts the time period used to determine whether a creditor is operating predominately in rural or underserved areas, from any of the three preceding calendar years to the preceding calendar year.

- **Providing additional implementation time for small creditors:** Eligible small creditors are currently able to make balloon-payment QM loans and balloon-payment high-cost mortgages regardless of where they operate, under a temporary exemption scheduled to expire on January 10, 2016. The CFPB's final rule extends that period to include balloon-payment mortgage transactions with applications received before April 1, 2016, giving creditors more time to understand how any changes will affect their status, and to adjust their business practices.

III. Effective Date

- The final rule is effective January 1, 2016.

[2] "Rural" is currently defined in the Regulation Z QM balloon and escrow exceptions as a county not in a metropolitan statistical area (MSA) and not in a micropolitan statistical area adjacent to an MSA.