Helping Credit Unions Serve Their Members

Comment Call (12-19)

To: All Affiliated Credit Union CEOs

From: Veronica Madsen – Director of Regulatory Affairs

Date: October 3, 2012

RE: CFPB – Appraisals for Higher-Risk Mortgages

Summary

The NCUA, along with the Federal Reserve Board (FRB), Consumer Financial Protection Bureau (CFPB), Federal Deposit Insurance Corporation (FDIC), Federal Housing Finance Agency (FHFA), and the Office of the Comptroller of the Currency, Treasury (OCC) propose to amend Regulation Z, which implements the Truth in Lending Act (TILA), and the official interpretation to the regulation.

The proposed revisions to Regulation Z would implement a new TILA provision requiring appraisals for "higher-risk mortgages" that was added to TILA as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).

For mortgages with an annual percentage rate (APR) that exceeds the average prime offer rate (APOR) by a specified percentage, the proposed rule would require creditors to obtain an appraisal or appraisals meeting certain specified standards, provide applicants with a notification regarding the use of the appraisals, and give applicants a copy of the written appraisals used.

A copy of the proposed rule can be found here: http://www.gpo.gov/fdsys/pkg/FR-2012-09-05/pdf/2012-20432.pdf.

Comments must be received on or before ***October 15, 2012***.

The Proposed Rule

Appraisals for Higher-Risk Mortgage Loans

Definitions

Certified or Licensed Appraiser - Consistent with TILA, the proposed rule would define "certified or licensed appraiser" as a person who is certified or licensed by the State agency in the State in which the property that secures the transaction is located, and who performs the appraisal in conformity with the Uniform Standards of Professional Appraisal Practice (USPAP) and the requirements applicable to appraisers in title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (FIRREA title XI), and any implementing regulations, in effect at the time the appraiser signs the appraiser's certification.

Should the rule address the issue of when a creditor must use a certified appraiser rather than a licensed appraiser? Should the rule address the issue of appraiser competency?

Higher-Risk Mortgage Loans - The proposed rule would define the term "higher-risk mortgage loan" as a closed-end consumer credit transaction secured by the consumer's principal dwelling with an APR that exceeds the APOR for a comparable transaction as of the date the interest rate is set by a specified percentage depending on the type of transaction.

The proposal uses the phrase "a closed-end consumer credit transaction secured by the consumer's principal dwelling" in place of the statutory term "residential mortgage loan," but incorporates the substantive elements of the "residential mortgage loan" definition into the proposed definition of "higher-risk mortgage loan."

"Higher-Risk Mortgage Loan" Versus "Higher-Priced Mortgage Loan"

The proposed rule would define a "higher-risk mortgage loan" as a closed-end consumer credit transaction secured by the consumer's principal dwelling with an APR that exceeds the APOR for a comparable transaction as of the date the interest rate is set by a specified percentage depending on the type of transaction. The proposed rule uses the phrase "a closed-end consumer credit transaction secured by the consumer's principal dwelling" in place of the statutory term "residential mortgage loan."

Do you think the terms "higher-risk mortgage loan" and "higher-priced mortgage loan" in different portions of Regulation Z will confuse industry or consumers and, if so, what alternative approach could the Agencies take to implementing the statutory definition of "higher-risk mortgage loan" consistent with the requirements of TILA?

In the CFPB's 2012 TILA–RESPA Proposal, the CFPB is proposing to adopt a simpler and more inclusive finance charge calculation for closed-end credit secured by real property or a dwelling. In light of the uncertainty regarding whether the CFPB will adopt such a finance charge and the potential impact of that change, the Agencies have proposed two alternative versions:

> *Alternative 1* would define the threshold for higher-risk mortgages based on APR. *Alternative 2* would use a transaction coverage rate (TCR). Under this approach, the TCR would be calculated in a manner similar to how the APR is calculated, except that the prepaid finance charge used for the TCR calculation would include only charges retained by the creditor, a mortgage broker, or an affiliate of either. The TCR would not reflect other closing costs that would be included in the broader finance charge for purposes of calculating the APR that would be disclosed to consumers. By excluding these fees, it is possible fewer loans would be covered by the rule.

As proposed, a higher-risk mortgage loan generally would be a closed-end consumer credit transaction secured by the consumer's principal dwelling with an APR (*Alternative 1*) / TCR (*Alternative 2*) that exceeds the APOR for a comparable transaction as of the date the interest rate is set:

- By 1.5% or more, for a loan secured by a first lien with a principal obligation at consummation that does not exceed the limit in effect as of the date the transaction's interest rate is set for the maximum principal obligation eligible for purchase by Freddie Mac;
- By 2.5% or more, for a loan secured by a first lien with a principal obligation at consummation that exceeds the limit in effect as of the date the transaction's interest rate is set for the maximum principal obligation eligible for purchase by Freddie Mac; and
- By 3.5% or more, for a loan secured by a subordinate lien.

Under the proposal, the following would be excluded from the definition of “higher-risk mortgage loan”:

- Any loan that is a “qualified mortgage” loan (this term remains undefined until the “Ability to Repay” proposal is finalized);
- A reverse-mortgage transaction;
- A loan secured solely by a residential structure. Thus, for example, a loan secured by a manufactured home and the land on which it is sited could be a “higher-risk mortgage loan.” By contrast, a loan secured solely by a manufactured home could not be a “higher-risk mortgage loan;”
- Construction loans; and
- Bridge loans.

Note: The Agencies would **not** adopt Alternative 2 if the CFPB does **not** change the definition of finance charge.

Questions:

- ***How can the CFPB account for the implications of a more inclusive finance charge on the scope of higher-risk mortgage coverage? Unlike the CFPB’s authority to adjust the threshold triggers in HOEPA, TILA section 129H does not give the Agencies express authority to revise the numeric threshold triggers for purposes of determining which loans are higher-risk mortgage loans.***

- ***What is the potential for the TCR to introduce additional complexity in enforcement and litigation contexts, and would this add to the burden on the industry?***

- ***What would be the impact of a more inclusive finance charge on the application of the higher-risk mortgage loan requirements?***

- ***Would it be in the public interest and promote the safety and soundness of creditors to modify the triggers for higher-risk mortgage loans to approximate more closely the coverage levels under the finance charge and APR as currently calculated?***

- ***If potential modifications are warranted, what methods would be appropriate, including use of the TCR in lieu of APR? What would be the relative costs and benefits of any modification in the context of the higher-risk mortgage loan appraisal proposal, including any potential impact on the market?***

[Where possible, comments should include supporting data. In particular, data regarding the amount of charges currently considered prepaid finance charges and the amount of charges currently excluded from the finance charge would enable the Agencies to make an informed assessment of the impacts a more inclusive finance charge would have on the higher-risk mortgage loan rule, and may be useful as well to the CFPB in considering other affected rules.]

Should construction and bridge loans be excluded from the definition of higher-risk mortgage loan? If not, would any additional compliance guidance be needed? Alternatively, should construction loans be exempt only from the requirement to conduct an interior visit of the property, and be subject to all other appraisal requirements under the proposed rule?

Should any other classes of loans should be excluded from the definition of higher-risk mortgage loan?

National Registry – The proposed rule would define this term to mean the database of information about State certified and licensed appraisers maintained by the Appraisal Subcommittee of the FFIEC.

State Agency – This term would mean a "State appraiser certifying and licensing agency" recognized in accordance with section 1118(b) of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) and any implementing regulations.

<u>Appraisals Required for Higher-Risk Mortgage Loans</u>

Under the proposed rule, a creditor could not extend a higher-risk mortgage loan to a consumer without obtaining, prior to consummation, a written appraisal performed by a certified or licensed appraiser who conducts a physical visit of the interior of the property that will secure the transaction.

Safe Harbor

The proposed rule would provide a safe harbor from this requirement when the appraiser certifies compliance with USPAP and applicable FIRREA title XI requirements. Specifically, under the safe harbor, a creditor would be deemed to have obtained a written appraisal that meets the requirements of the rule if the creditor does the following:

- Orders that the appraiser perform the appraisal in conformity with USPAP and FIRREA title XI, and any implementing regulations, in effect at the time the appraiser signs the appraiser's certification;
- Verifies through the National Registry that the appraiser who signed the appraiser's certification holds a valid appraisal license or certification in the State in which the appraised property is located;
- Confirms that the elements set forth in Appendix N to Regulation Z are addressed in the written appraisal; and
- Has no actual knowledge to the contrary of facts or certifications contained in the written appraisal.

Proposed Appendix N to part 1026 provides that, to qualify for the safe harbor, a creditor would be required to check to confirm that the written appraisal:

- Identifies the creditor who ordered the appraisal and the property and the interest being appraised.
- Indicates whether the contract price was analyzed.
- Addresses conditions in the property's neighborhood.
- Addresses the condition of the property and any improvements to the property.
- Indicates which valuation approaches were used, and includes a reconciliation if more than one valuation approach was used.
- Provides an opinion of the property's market value and an effective date for the opinion.
- Indicates that a physical property visit of the interior of the property was performed.
- Includes a certification signed by the appraiser that the appraisal was prepared in accordance with the requirements of USPAP.
- Includes a certification signed by the appraiser that the appraisal was prepared in accordance with the requirements of FIRREA title XI, as amended, and any implementing regulations.

The proposed rule would **not** require the creditor to make any independent judgment about or perform any independent analysis of the conclusions and factual statements in the written appraisal.

What do you think is the appropriateness of the safe harbor, the list of requirements a creditor must satisfy to receive the safe harbor and Appendix N? Should the proposed safe harbor be included in the rule?

Additional Appraisal for Certain Higher-Risk Mortgage Loans

Under the proposed rule, a creditor would be required to obtain an additional appraisal from a different certified or licensed appraiser if the higher-risk mortgage loan will finance the acquisition of the mortgaged property from a seller within 180 days of the purchase or acquisition of such property by the seller at a price that was lower than the current sale price of the property. This approach is consistent the Department of Housing and Urban Development (HUD) regulations that address property flipping in single-family mortgage insurance programs of the Federal Housing Administration (FHA).

A creditor would have the discretion to select the most reliable valuation, consistent with applicable safety and soundness obligations and prudential guidance. The proposal also notes that, if the creditor is required to obtain two appraisals, it may charge the consumer for only one of the appraisals.

The proposed comment would clarify that an appraisal previously obtained in connection with the seller's acquisition or the financing of the seller's acquisition of the property could **not** be used as one of the two required appraisals.

Potential Exemptions from the Additional Appraisal Requirement

TILA permits the Agencies to jointly exempt a class of loans from the additional appraisal requirement if the Agencies determine the exemption "is in the public interest and promotes the safety and soundness of creditors." Exemptions to be considered may include higher-risk mortgage loans made in rural areas where finding two independent appraisers may be difficult, as well as the types of transactions that are currently exempted from the restrictions on FHA insurance applicable to property re-sales in the FHA Anti- Flipping Rule (including, among others, sales by government agencies of certain properties, sales of properties acquired by inheritance, and sales by state- and federally-chartered financial institutions).

What are your thoughts on this? Should the rule use the same definition of "rural" that is provided in the 2011 Ability to Repay Proposal (i.e., based on the "urban influence codes" numbered 7, 10, 11, and 12, maintained by the Economic Research Service (ERS) of the United States Department of Agriculture)? ***How would such an exemption serve the public interest and promote the safety and soundness of creditors?***

Acquisition of the Consumer's Principal Dwelling

Higher-risk mortgage loans are defined by TILA as loans secured by a consumer's principal dwelling. Thus, the additional appraisal requirement would **not** apply to refinances, home-equity loans, or subordinate liens that do not finance the consumer's acquisition of a principal dwelling.

If the rule were to cover non-purchase acquisitions by the consumer, how should a creditor calculate the consumer's "sale price"? Should the term "acquisition" be clarified to address situations in which a consumer previously held a partial interest in the property, and is acquiring the remainder of the interest from the seller?

Is the term "acquisition" the appropriate term to use in connection with both the seller and higher-risk mortgage consumer? The Agencies may further clarify the term or use a different term, such as "purchase."

To implement this provision, the proposal would require the creditor to compare (1) the date on which the consumer entered into the agreement to acquire the property from the seller, and (2) the date on which the seller acquired the property. In determining this date, the creditor should use a copy of the agreement itself provided by the consumer to the creditor, and use the date on which the consumer and the seller signed the agreement. If the two dates are different, the creditor should use the date on which the last party signed the agreement.

Criteria for Whether an Additional Appraisal is Required - Acquisition Price

The creditor would be required to compare the price paid by the seller to acquire the property with the price that the consumer is obligated to pay to acquire with property, as specified in the consumer's agreement to acquire the property.

The creditor would have to consider only the price of the property - **not** the total cost of financing the property.

How would a creditor calculate the price paid by a seller to acquire a property as part of a bulk sale that is later resold to a higher-risk mortgage consumer? What operational challenges would arise for creditors in determining purchase prices for homes purchased as part of a bulk sale transaction? Should a bulk sale be an exception to the additional appraisal requirement?

Exemption for small price increases. The Agencies propose an exemption from the additional appraisal requirement for relatively small increases in the price. Although the proposal does **not** contain a particular price threshold, the Agencies may develop one in the final rule based on public comments received in response to this proposal.

What would an appropriate threshold be, rather than provide a particular amount or formula in the proposal? A fixed dollar amount, a fixed percentage, or some alternate approach? The Agencies request that commenters support their recommendations with specific data, where possible.

Requirements for the Additional Appraisal

The following requirements for the additional appraisal would apply:

- It would have to be performed by a "different" certified or licensed appraiser;
- It would have to be performed by a certified or licensed appraiser who conducts a physical visit of the interior of the mortgaged property;
- It would have to include an analysis of several elements, including any improvements made to the property between the date of the previous sale and the current sale;
- It would have to include an analysis of the difference between the price at which the seller acquired the property and the price the consumer is obligated to pay to acquire the property, as specified in the consumer's acquisition agreement; and
- It would have to include an analysis of changes in market conditions and improvements made to the property between the date of the seller's acquisition of the property and the date of the consumer's agreement to acquire the property.

Inability to Make the Determination

The proposed rule would require a higher-risk mortgage loan creditor that cannot determine the seller's acquisition date or price to obtain an additional appraisal. However, the additional appraisal in this situation would not have to contain the full analysis required for additional appraisals of flipping transactions. An analysis of the elements would only be required to the extent that the creditor knows the seller's purchase price and acquisition date.

Under this proposal, when information about a property is not available from written source documents, creditors extending higher-risk mortgage loans will routinely incur increased costs associated with obtaining the additional appraisal. One risk of the proposal is that creditors will simply refrain from engaging in any higher-risk mortgage loan transaction where sales history data cannot be obtained. In "non-disclosure" jurisdictions, where property sales price information is routinely unavailable through public records, this requirement could limit the availability of higher-risk mortgage loans.

Would the enhanced protections for consumers afforded by requiring an additional appraisal whenever the seller's acquisition date or price cannot be determined merit the potential restraint on the availability of higher-risk mortgage loans?

Required Disclosure

The proposed rule would require the following disclosure: "We may order an appraisal to determine the property's value and charge you for this appraisal. We will promptly give you a copy of any appraisal, even if your loan does not close. You can pay for an additional appraisal for your own use at your own cost."

Should any changes be made to the text of the notification to further enhance consumer comprehension?

The proposed comment would clarify that when two or more consumers apply for a loan subject to this section, the creditor is required to give the disclosure to only one of the consumers.

Timing of Disclosure

The proposed rule would require that the disclosure be delivered not later than the 3rd business day after the creditor receives the consumer's application.

Would providing the notification at some other time would be more beneficial to consumers, and how should it be provided when an application is submitted by telephone, facsimile or electronically?

Should creditors who have a reasonable belief that the transaction will not be a higher-risk mortgage loan at the time of application, but later determine that the applicant only qualifies for a higher-risk mortgage loan, be allowed an opportunity to cure and give the required disclosure at some later time in the application process?

Copy of Appraisals

The proposal would require a creditor to provide a copy of any written appraisal performed in connection with a higher-risk mortgage loan to the applicant. When two or more consumers apply for a loan subject to this section, the creditor would be required to give the copy of required appraisals to only one of the consumers.

Timing

The proposed rule would require creditors to provide copies of written appraisals no later than 3 business days prior to consummation of the higher-risk mortgage loan.

Form of Copy

The proposed rule would allow a copy of a written appraisal to be provided to the applicant in electronic form, subject to compliance with the consumer consent and other applicable provisions of the E-Sign Act.

No Charge for Copy of Appraisal

Under the proposed rule, a creditor could **not** charge the applicant for a copy of a required written appraisal by imposing a fee specifically for a required copy of an appraisal or by marking up the interest rate or any other fees payable by the consumer in connection with the higher-risk mortgage loan.

Comment Letters

Interested parties are encouraged to submit written comments jointly to all of the Agencies. Commenters are encouraged to use the title "Appraisals for Higher-Risk Mortgage Loans" to facilitate the organization and distribution of comments among the Agencies.

Please submit a Comment Letter to:

Monica Jackson
Office of the Executive Secretary
Bureau of Consumer Financial Protection
1700 G Street NW.
Washington, DC 20552.

Identify your letter by Docket No. CFPB–2012–0031.

Electronic: http://www.regulations.gov. Follow the instructions for submitting comments. Include RIN 3170–AA11 in the submission. Refer to Docket Number CFPB-2012–0031.

Please submit to MCUL a copy of your response to the attention of:

Veronica Madsen
Director of Regulatory Affairs
Michigan Credit Union League & Affiliates
38695 W. Seven Mile Road, Suite 200
Livonia, MI 48152-7097

E-mail: veronica.madsen@mcul.org

Fax: (734) 793-7155

We Appreciate Your Response.