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DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

12 CFR Parts 34 and 164

[Docket No. OCC-2012-0013]

RIN 1557-AD62

BOARD OF GOVERNORS OF FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Docket No. R-1443]

RIN 7100-AD90

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 722

RIN 3133-AE04

BUREAU OF CONSUMER FINANCIAL PROTECTION

12 CFR Part 1026

[Docket No. CFPB-2012-0031]

RIN 3170-AA11

FEDERAL HOUSING FINANCE AGENCY

12 CFR Part 1222

RIN 2590-AA58

Appraisals for Higher-Priced Mortgage Loans

AGENCIES: Board of Governors of the Federal Reserve System (Board); Bureau of Consumer Financial Protection (Bureau); Federal Deposit Insurance Corporation (FDIC); Federal Housing Finance Agency (FHFA); National Credit Union Administration (NCUA); and Office of the Comptroller of the Currency, Treasury (OCC).

ACTION: Final rule; official staff commentary.

SUMMARY: The Board, Bureau, FDIC, FHFA, NCUA, and OCC (collectively, the Agencies) are issuing a final rule to amend Regulation Z, which implements the Truth in Lending Act (TILA), and the official interpretation to the regulation. The revisions to Regulation Z implement a new provision requiring appraisals for "higher-risk mortgages" that was added to TILA by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act or Act). For mortgages with an annual percentage rate that exceeds the average prime offer rate by a specified percentage, the final rule requires 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.

EFFECTIVE DATES: This final rule is effective on January 18, 2014.

FOR FURTHER INFORMATION CONTACT:

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Banking Supervision and Regulation, at (202) 973-6122, Board of Governors of the Federal Reserve System, Washington, DC 20551.

Bureau: Owen Bonheimer, Counsel, or William W. Matchneer, Senior Counsel, Division of Research, Markets, and Regulations, Bureau of Consumer Financial Protection, 1700 G Street, N.W., Washington, DC 20552, at (202) 435-7000.

FDIC: Beverlea S. Gardner, Senior Examination Specialist, Risk Management Section, at (202) 898-3640, Sumaya A. Muraywid, Examination Specialist, Risk Management Section, at (573) 875-6620, Glenn S. Gimble, Senior Policy Analyst, Division of Consumer Protection, at (202) 898-6865, Sandra S. Barker, Senior Policy Analyst, Division of Consumer Protection, at (202 898-3615, Mark Mellon, Counsel, Legal Division, at (202) 898-3884, or Kimberly Stock, Counsel, Legal Division, at (202) 898-3815, or 550 17th St, N.W., Washington, DC 20429.

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NCUA: John Brolin and Pamela Yu, Staff Attorneys, or Frank Kressman, Associate General Counsel, Office of General Counsel, at (703) 518-6540, or Vincent Vieten, Program Officer, Office of Examination and Insurance, at (703) 518-6360, or 1775 Duke Street, Alexandria, Virginia, 22314.

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SUPPLEMENTARY INFORMATION:

I. Background

In general, the Truth in Lending Act (TILA), 15 U.S.C. 1601 *et seq*., seeks to promote the informed use of consumer credit by requiring disclosures about its costs and terms. TILA requires additional disclosures for loans secured by consumers' homes and permits consumers to rescind certain transactions that involve their principal dwelling. For most types of creditors, TILA directs the Bureau to prescribe regulations to carry out the purposes of the law and specifically authorizes the Bureau to issue regulations that contain such classifications, differentiations, or other provisions, or that provide for such adjustments and exceptions for any class of transactions, that in the Bureau's judgment are necessary or proper to effectuate the purposes of TILA, or prevent circumvention or evasion of TILA.[1] 15 U.S.C. 1604(a). For most types of creditors and most provisions of the statute, TILA is implemented by the Bureau's Regulation Z. *See* 12 CFR part 1026. Official Interpretations provide guidance to creditors in applying the rules to specific transactions and interpret the requirements of the regulation. *See* 12 CFR part 1026, Supp. I. However, as explained in the section-by-section analysis of this **SUPPLEMENTARY INFORMATION**, the new appraisal section of TILA addressed in this final rule (TILA section 129H, 15 U.S.C. 1639h) is implemented not only for all affected

[1] For motor vehicle dealers as defined in section 1029 of the Dodd-Frank Act, TILA directs the Board to prescribe regulations to carry out the purposes of TILA and authorizes the Board to issue regulations that contain such classifications, differentiations, or other provisions, or that provide for such adjustments and exceptions for any class of transactions, that in the Board's judgment are necessary or proper to effectuate the purposes of TILA, or prevent circumvention or evasion of TILA. 15 U.S.C. 5519; 15 U.S.C. 1604(a).

creditors by the Bureau's Regulation Z, but also, for creditors overseen by the OCC and the Board, respectively, by OCC regulations and the Board's Regulation Z. *See* 12 CFR parts 34 and 164 (OCC regulations) and part 226 (the Board's Regulation Z). The Bureau's, the OCC's and the Board's versions of the appraisal rules and corresponding official interpretations are substantively identical. The FDIC, NCUA, and FHFA are adopting the Bureau's version of the regulations under this final rule.

The Dodd-Frank Act[2] was signed into law on July 21, 2010. Section 1471 of the Dodd-Frank Act's Title XIV, Subtitle F (Appraisal Activities), added a new TILA section 129H, 15 U.S.C. 1639h, which establishes appraisal requirements that apply to "higher-risk mortgages." Specifically, new TILA section 129H prohibits a creditor from extending credit in the form of a higher-risk mortgage loan to any consumer without first:

- Obtaining a written appraisal performed by a certified or licensed appraiser who conducts a physical property visit of the interior of the property.
- Obtaining an additional appraisal from a different certified or licensed appraiser if the higher-risk mortgage finances the purchase or acquisition of a property from a seller at a higher price than the seller paid, within 180 days of the seller's purchase or acquisition. The additional appraisal must include an analysis of the difference in sale prices, changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale.

A creditor of a "higher-risk mortgage" must also:

[2] Public Law 111-203, 124 Stat. 1376 (Dodd-Frank Act).

- Provide the applicant, at the time of the initial mortgage application, with a statement that any appraisal prepared for the mortgage is for the sole use of the creditor, and that the applicant may choose to have a separate appraisal conducted at the applicant's expense.
- Provide the applicant with one copy of each appraisal conducted in accordance with TILA section 129H without charge, at least three (3) days prior to the transaction closing date.

New TILA section 129H(f) defines a "higher-risk mortgage" with reference to the annual percentage rate (APR) for the transaction. A higher-risk mortgage is a "residential mortgage loan"[3] secured by a principal dwelling with an APR that exceeds the average prime offer rate (APOR) for a comparable transaction as of the date the interest rate is set—

- By 1.5 or more percentage points, for a first lien residential mortgage loan with an original principal obligation amount that does not exceed the amount for the maximum limitation on the original principal obligation of a mortgage in effect for a residence of the applicable size, as of the date of the interest rate set, pursuant to the sixth sentence of section 305(a)(2) of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1454);
- By 2.5 or more percentage points, for a first lien residential mortgage loan having an original principal obligation amount that exceeds the amount for the maximum limitation on the original principal obligation of a mortgage in effect for a residence of the applicable size, as of the date of the interest rate set, pursuant to the sixth sentence of section 305(a)(2) of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1454); or

[3] *See* Dodd-Frank Act, § 1401; TILA section 103(cc)(5), 15 U.S.C. 1602(cc)(5) (defining "residential mortgage loan").

- By 3.5 or more percentage points, for a subordinate lien residential mortgage loan.

The definition of “higher-risk mortgage” expressly excludes “qualified mortgages,” as defined in TILA section 129C, and “reverse mortgage loans that are qualified mortgages,” as defined in TILA section 129C. 15 U.S.C. 1639c.

New TILA section 103(cc)(5) defines the term “residential mortgage loan” as any consumer credit transaction that is secured by a mortgage, deed of trust, or other equivalent consensual security interest on a dwelling or on residential real property that includes a dwelling, other than a consumer credit transaction under an open-end credit plan. 15 U.S.C. 1602(cc)(5).

New TILA section 129H(b)(4)(A) requires the Agencies jointly to prescribe regulations to implement the property appraisal requirements for higher-risk mortgages. 15 U.S.C. 1639h(b)(4)(A). The Dodd-Frank Act requires that final regulations to implement these provisions be issued within 18 months of the transfer of functions to the Bureau pursuant to section 1062 of the Act, or January 21, 2013.[4] These regulations are to take effect 12 months after issuance.[5]

The Agencies published proposed regulations on September 5, 2012, that would implement these higher-risk mortgage appraisal provisions. 77 FR 54722 (Sept. 5, 2012). The comment period closed on October 15, 2012. The Agencies received more than 200 comment letters regarding the proposal from banks, credit unions, other creditors, appraisers, appraisal management companies, industry trade associations, consumer groups, and others.

[4] *See* Dodd-Frank Act, § 1400(c)(1).
[5] *See id.*

II. Summary of the Final Rule

Loans Covered

To implement the statutory definition of "higher-risk mortgage," the final rule uses the term "higher-priced mortgage loan" (HPML), a term already in use under the Bureau's Regulation Z with a meaning substantially similar to the meaning of "higher-risk mortgage" in the Dodd-Frank Act. In response to commenters, the Agencies are using the term HPML to refer generally to the loans that could be subject to this final rule because they are closed-end credit and meet the statutory rate triggers, but the Agencies are separately exempting several types of HPML transactions from the rule. The term "higher-risk mortgage" encompasses a closed-end consumer credit transaction secured by a principal dwelling with an APR exceeding certain statutory thresholds. These rate thresholds are substantially similar to rate triggers that have been in use under Regulation Z for HPMLs.[6] Specifically, consistent with TILA section 129H, a loan is a "higher-priced mortgage loan" under the final rule if the APR exceeds the APOR by 1.5 percent for first-lien conventional or conforming loans, 2.5 percent for first-lien jumbo loans, and 3.5 percent for subordinate-lien loans.[7]

Consistent with the statute, the final rule exempts "qualified mortgages" from the requirements of the rule. Qualified mortgages are defined in § 1026.43(e) of the Bureau's final rule implementing the Dodd-Frank Act's ability-to-repay requirements in TILA section 129C (2013 ATR Final Rule).[8] 15 U.S.C. 1639c.

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[6] Added to Regulation Z by the Board pursuant to the Home Ownership and Equity Protection Act of 1994 (HOEPA), the HPML rules address unfair or deceptive practices in connection with subprime mortgages. *See* 73 FR 44522, July 30, 2008; 12 CFR 1026.35.

[7] The existing HPML rules apply the 2.5 percent over APOR trigger for jumbo loans only with respect to a requirement to establish escrow accounts. *See* 12 CFR 1026.35(b)(3)(v).

[8] The Bureau released the 2013 ATR Final Rule on January 10, 2013, under Docket No. CFPB-2011-0008, CFPB-2012-0022, RIN 3170-AA17, at http://consumerfinance.gov/Regulations.

In addition, the final rule excludes the following classes of loans from coverage of the higher-risk mortgage appraisal rule:

(1) transactions secured by a new manufactured home;

(2) transactions secured by a mobile home, boat, or trailer;

(3) transactions to finance the initial construction of a dwelling;

(4) loans with maturities of 12 months or less, if the purpose of the loan is a "bridge" loan connected with the acquisition of a dwelling intended to become the consumer's principal dwelling; and

(5) reverse mortgage loans.

For reasons discussed more fully in the section-by-section analysis of § 1026.35(a)(1), below, the proposal included a request for comments on an alternative method of determining coverage based on the "transaction coverage rate" or TCR, rather than the APR. Unlike the APR, the TCR would exclude all prepaid finance charges not retained by the creditor, a mortgage broker, or an affiliate of either.[9] This change was proposed to address a possible expansion of the definition of "finance charge" used to calculate the APR, proposed by the Bureau in its rulemaking to integrate mortgage disclosures (2012 TILA-RESPA Proposal[10]). Accordingly, the proposal defined "higher-risk mortgage loan" (termed "higher-priced mortgage loan" in this final rule) in the alternative as calculated by either the TCR or APR, with comment sought on both approaches.

As explained more fully in the section-by-section analysis of § 1026.35(a)(1), below, the final rule requires creditors to determine whether a loan is an HPML by comparing the APR to the APOR. The Agencies are not at this time adopting the proposed alternative of replacing the

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[9] *See* 75 FR 58539, 58660-62 (Sept. 24, 2010); 76 FR 11598, 11609, 11620, 11626 (March 2, 2011).
[10] *See* 77 FR 51116 (Aug. 23, 2012).

APR with the TCR and comparing the TCR to the APOR. The Agencies will consider the merits of any modifications to this approach and public comments on this matter if and when the Bureau adopts the more inclusive definition of finance charge proposed in the 2012 TILA-RESPA Proposal.

Finally, based on public comments, the Agencies intend to publish a supplemental proposal to request comment on possible exemptions for "streamlined" refinance programs and small dollar loans, as well as to seek comment on whether application of the HPML appraisal rule to loans secured by certain other property types, such as existing manufactured homes, is appropriate.

Requirements that Apply to All Appraisals Performed for Non-Exempt HPMLs

Consistent with the statute, the final rule allows a creditor to originate an HPML that is not otherwise exempt from the appraisal rules only if the following conditions are met:

- The creditor obtains a written appraisal;
- The appraisal is performed by a certified or licensed appraiser; and
- The appraiser conducts a physical property visit of the interior of the property.

Also consistent with the statute, the following requirements also apply with respect to HPMLs subject to the final rule:

- At application, the consumer must be provided with a statement regarding the purpose of the appraisal, that the creditor will provide the applicant a copy of any written appraisal, and that the applicant may choose to have a separate appraisal conducted for the applicant's own use at his or her own expense; and
- The consumer must be provided with a free copy of any written appraisals obtained for the transaction at least three (3) business days before consummation.

Requirement to Obtain an Additional Appraisal in Certain HPML Transactions

In addition, the final rule implements the Act's requirement that the creditor of a "higher-risk mortgage" obtain an additional written appraisal, at no cost to the borrower, when the "higher-risk mortgage" will finance the purchase of the consumer's principal dwelling and there has been an increase in the purchase price from a prior sale that took place within 180 days of the current sale. TILA section 129H(b)(2)(A), 15 U.S.C. 1639(b)(2)(A). In the final rule, using their exemption authority, the Agencies are setting thresholds for the increase that will trigger an additional appraisal. An additional appraisal will be required for an HPML (that is not otherwise exempt) if either:

- The seller is reselling the property within 90 days of acquiring it and the resale price exceeds the seller's acquisition price by more than 10 percent; or
- The seller is reselling the property within 91 to 180 days of acquiring it and the resale price exceeds the seller's acquisition price by more than 20 percent.

The additional written appraisal, from a different licensed or certified appraiser, generally must include the following information: an analysis of the difference in sale prices (*i.e.*, the sale price paid by the seller and the acquisition price of the property as set forth in the consumer's purchase agreement), changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale.

III. Legal Authority

As noted above, TILA section 129H(b)(4)(A), added by the Dodd-Frank Act, requires the Agencies jointly to prescribe regulations implementing section 129H. 15 U.S.C. 1639h(b)(4)(A). In addition, TILA section 129H(b)(4)(B) grants the Agencies the authority jointly to exempt, by rule, a class of loans from the requirements of TILA section 129H(a) or section 129H(b) if the

Agencies determine that the exemption is in the public interest and promotes the safety and soundness of creditors. 15 U.S.C. 1639h(b)(4)(B).

IV. Section-by-Section Analysis

For ease of reference, unless otherwise noted, the **SUPPLEMENTARY INFORMATION** refers to the section numbers of the rules that will be published in the Bureau's Regulation Z at 12 CFR 1026.35(a) and (c).[11] As explained further in the section-by-section analysis of § 1026.35(c)(7), the rules are being published separately by the OCC, the Board, and the Bureau. No substantive difference among the three sets of rules is intended. The NCUA and FHFA adopt the rules as published in the Bureau's Regulation Z at 12 CFR 1026.35(a) and (c), by cross-referencing these rules in 12 CFR 722.3 and 12 CFR Part 1222, respectively. The FDIC adopts the rules as published in the Bureau's Regulation Z at 12 CFR 1026.35(a) and (c), but does not cross-reference the Bureau's Regulation Z.

Section 1026.35 Prohibited Acts or Practices in Connection with Higher-Priced Mortgage Loans

The final rule is incorporated into Regulation Z's existing section on prohibited acts or practices in connection with HPMLs, § 1026.35. As revised, § 1026.35 will consist of four subsections – (a) Definitions; (b) Escrows for higher-priced mortgage loans; (c) Appraisals for higher-priced mortgage loans; and (d) Evasion; open-end credit. As explained in more detail in the Bureau's final rule on escrow requirements for HPMLs (2013 Escrows Final Rule)[12] (finalizing the Board's proposal to implement the Act's escrow account requirements under TILA section 129D, 15 U.S.C. 1639d (2011 Escrows Proposal)[13]), the subsections on repayment ability (existing § 1026.35(b)(1)) and prepayment penalties (existing § 1026.35(b)(2)) will be

[11]The final rule was issued by the Bureau on January 18, 2013, in accordance with 12 CFR 1074.1.
[12] The Bureau released the 2013 Escrows Final Rule on January 10, 2013, under Docket No. CFPB-2013-0001, RIN 3170-AA16, at http://consumerfinance.gov/Regulations.
[13] 76 FR 11598, 11612 (March 2, 2011).

deleted because the Dodd-Frank Act addressed these matters in other ways. Accordingly, repayment ability and prepayment penalties are now addressed in the Bureau's final ability-to-repay rule (2013 ATR Final Rule) and high-cost mortgage rule (2013 HOEPA Final Rule).[14] *See* §§ 1026.32(d)(6) and 1026.43(c), (d), (f), and (g).

35(a) Definitions

35(a)(1) Higher-priced mortgage loan

TILA section 129H(f) defines a "higher-risk mortgage" as a residential mortgage loan secured by a principal dwelling with an APR that exceeds the APOR for a comparable transaction by a specified percentage as of the date the interest rate is set. 15 U.S.C. 1639(f). New TILA section 103(cc)(5) defines the term "residential mortgage loan" as "any consumer credit transaction that is secured by a mortgage, deed of trust, or other equivalent consensual security interest on a dwelling or on residential real property that includes a dwelling, other than a consumer credit transaction under an open-end credit plan." 15 U.S.C. 1602(cc)(5).

Consistent with TILA sections 129H(f) and 103(cc)(5), the proposal provided that a "higher-risk mortgage loan" is 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 1.5 percentage points for first-lien conventional mortgages, 2.5 percentage points for first-lien jumbo mortgages, and 3.5 percentage points for subordinate-lien mortgages.

The Agencies noted in the proposal that the statutory definition of higher-risk mortgage, though similar to that of the regulatory term "higher-priced mortgage loan," differs from the existing regulatory definition of higher-priced mortgage loan in some important respects. First,

[14] The Bureau released the 2013 HOEPA Final Rule on January 10, 2013, under Docket No. CFPB-2012-0029, RIN 3170-AA12, at http://consumerfinance.gov/Regulations.

the statutory definition of higher-risk mortgage expressly excludes loans that meet the definition of a "qualified mortgage" under TILA section 129C. In addition, the statutory definition of higher-risk mortgage includes an additional 2.5 percentage point threshold for first-lien jumbo mortgage loans, while the definition of higher-priced mortgage loan has contained this threshold only for purposes of applying the requirement to establish escrow accounts for higher-priced mortgage loans. *Compare* TILA section 129H(f)(2), 15 U.S.C. 1639h(f)(2), *with* 12 CFR 1026.35(a)(1) and 1026.35(b)(3). The Agencies requested comment on whether the concurrent use of the defined terms "higher-risk mortgage loan" and "higher-priced mortgage loan" in different portions of Regulation Z may confuse industry or consumers and, if so, what alternative approach the Agencies could take to implementing the statutory definition of "higher-risk mortgage loan" consistent with the requirements of TILA section 129H. 15 U.S.C. 1639h.

The final rule adopts the proposed definition, but replaces the term "higher-risk mortgage loan" with the term "higher-priced mortgage loan" or HPML. *See* existing § 1026.35(a)(1). The final rule also makes certain changes to the existing definition of HPML, discussed in detail below.

Public Comments on the Proposal

Several credit unions, banks, and an individual commenter believed that the definition of "higher-risk mortgage loan" did not adequately capture loans that were truly "high risk." Several of these commenters stated that the definition should account not only for the cost of the loan, but also for other risk factors, such as debt to income ratio, loan amounts, and credit scores and other measures of a consumer's creditworthiness. A bank commenter believed that the interest rate thresholds in the definition were ambiguous and arbitrary and asserted that, for example, 1.5 percent was not an exceptionally high interest margin in comparison with interest margins for credit cards and other financing. A credit union commenter believed the rule would apply to consumers who were in fact a low credit risk.

Most commenters on the definition expressly supported using the existing term HPML rather than the new term "higher-risk mortgage loan." Commenters including, among others, a mortgage company, bank, credit union, financial holding company, credit union trade association, and banking trade association, asserted that the use of two terms with similar meanings would be confusing to the mortgage credit industry. Some asserted that consumers would be confused by this as well. Some of these commenters noted that Regulation Z also already used the term "high-cost mortgage" with different requirements and believed this third term would further compound consumer and industry confusion. Of commenters who expressed a preference for the term that should be used, most recommended using the term HPML because this term has been used by industry for some time.

Some commenters on this issue also advocated making the rate triggers and overall definition the same for existing HPMLs and "higher-risk mortgages" regardless of the terms used. They argued that this would reduce compliance burdens and confusion and ease costs associated with developing and managing systems. One commenter believed that developing a single standard would also avoid creating unnecessary delay and additional cost for consumers in the origination process.

A few commenters acknowledged key differences between the statutory meaning of "higher-risk mortgage" and the regulatory term HPML, and suggested ways of harmonizing the two definitions. For example, these commenters noted that "higher-risk mortgages" do not include qualified mortgages, whereas HPMLs do. To address this difference, one commenter suggested, for example, that the appraisal requirements should apply to HPMLs as currently defined, except for qualified mortgages. Other commenters suggested that the basic definition of HPML be understood to refer solely to the rate thresholds and suggested that the exemption for qualified mortgages from the appraisal rules be inserted as a separate provision. They did not discuss how to address additional variances in the types of transactions excluded from HPML and "higher-risk mortgage," respectively, such as the exclusion from the meaning of HPML but not the statutory definition of "higher-risk mortgage" for construction-only and bridge loans.

Other commenters also acknowledged that the current definition of HPML includes only two rate thresholds – one for first-lien mortgages (APR exceeds APOR by 1.5 percentage points) and the other for subordinate-lien mortgages (APR exceeds APOR by 3.5 percentage points). By contrast, the statutory definition of "higher-risk mortgage" has an additional rate tier for first-lien jumbo mortgages (APR exceeds APOR by 2.5 percentage points). The HPML requirements in Regulation Z apply a rate threshold of 2.5 percentage points above APOR to jumbo loans only for purposes of the requirement to escrow. The commenters who noted this distinction held the view that the "middle tier" threshold would not have a practical advantage for lenders or consumers. Instead, they recommended adopting a final rule with a single APR trigger of 1.5 percentage points above APOR for all first-lien loans.

Discussion

In the final rule, the Agencies use the term HPML rather than the proposed term "higher-risk mortgage loan" to refer generally to the loans covered by the appraisal rules. In a separate subsection of the final rule (§ 1026.35(c)(2), discussed in the section-by-section analysis below), the Agencies exempt several types of transactions from coverage of the HPML appraisal rules.

On January 10, 2013, the Bureau published the 2013 Escrows Final Rule, its final rule to implement Dodd-Frank Act amendments to TILA regarding the requirement to escrow for certain consumer mortgages.[15] *See* TILA section 129D, 15 U.S.C. 1639d. These rules are to take effect in May 2013, before the effective date of this final rule (January 18, 2014).

Thus, consistent with TILA sections 129H(f) and 103(cc)(5) and the proposal, the final rule in § 1026.35(a)(1) follows the Bureau's 2013 Escrows Final Rule in defining an HPML as a closed-end consumer credit transaction secured by the consumer's principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set:

- By 1.5 or more percentage points, 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 percentage points, 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 percentage points, for a loan secured by a subordinate lien.

The Agencies acknowledge that some commenters have concerns about the rate thresholds; however, these rate thresholds are prescribed by statute. *See* TILA section 129H(f)(2), 15 U.S.C. 1639h(f)(2); *see also* 15 U.S.C. 1602(cc)(5).

The Bureau in the 2013 Escrows Final Rule adopted a definition of HPML that is consistent for both TILA's escrow requirement and TILA's appraisal requirements for "higher-risk mortgages." TILA sections 129D and 129H, 15 U.S.C. 1639d and 1639h. This definition

[15] The Bureau released the 2013 Escrows Final Rule on January 10, 2013, under Docket No. CFPB-2013-0001, RIN 3170-AA16, at http://consumerfinance.gov/Regulations.

incorporates the APR thresholds for loans covered by these rules as prescribed by Dodd-Frank Act amendments to TILA and also reflects that both sets of rules apply only to closed-end mortgage transactions. TILA sections 129D(b)(3) and 129H(f), 15 U.S.C. 1639d(b)(3) and 1639h(f). Overall, the revised definition of HPML adopted in the 2013 Escrows Final Rule reflects only minor changes from the current definition of HPML in existing 12 CFR 1026.35(a). For clarity, the Agencies are re-publishing the definition published earlier in the 2013 Escrows Final Rule.[16] The incorporation by reference in § 1026.35(c) of the term HPML in § 1026.35(a) and the re-publishing of § 1026.35(a) in this final rule are not intended to subject § 1026.35(a) to the joint rulemaking authority of the Agencies under TILA section 129H.

Consistent with the proposal, the final 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" throughout § 1026.35(a)(1). As also proposed, the Agencies have elected to incorporate the substantive elements of the statutory definition of "residential mortgage loan" into the definition of HPML rather than using the term itself to avoid inadvertent confusion of the term "residential mortgage loan" with the term "residential mortgage transaction," which is an established term used throughout Regulation Z and defined in § 1026.2(a)(24). *Compare* 15 U.S.C. 1602(cc)(5) (defining "residential mortgage loan") *with* 12 CFR 1026.2(a)(24) (defining "residential mortgage transaction"). Accordingly, the final regulation text differs from the express statutory language, but with no intended substantive change to the scope of TILA section 129H.

Annual Percentage Rate (APR) versus Transaction Coverage Rate (TCR)

[16] In their respective publications of the final rule, the Board is publishing the definition of HPML at 12 CFR 226.43(a)(3) and the OCC is including a cross-reference to the definition of HPML at 12 CFR 34.202(b).

The Agencies are not at this time adopting an alternative method of determining coverage based on the "transaction coverage rate" or TCR. The proposal included a request for comments on a proposed amendment to the method of calculating the APR that was proposed as part of other mortgage-related proposals issued for comment by the Bureau. In the Bureau's proposal to integrate mortgage disclosures (2012 TILA-RESPA Proposal), the Bureau proposed to adopt a more simple and inclusive finance charge calculation for closed-end credit secured by real property or a dwelling.[17] The more-inclusive finance charge definition would affect the APR calculation because the finance charge is integral to the APR calculation. The Bureau therefore also sought comment on whether replacing APR with an alternative metric might be warranted to determine whether a loan is a "high-cost mortgage" covered by the Bureau's proposal to implement the Dodd-Frank Act provision related to "high-cost mortgages" (2012 HOEPA Proposal),[18] as well as by the proposal to implement the Dodd-Frank Act's escrow requirements in TILA section 129D (2011 Escrows Proposal).[19] The alternative metric would have implications for the 2013 ATR Final Rule as well. One possible alternative metric discussed in those proposals is the "transaction coverage rate" (TCR), which would exclude all prepaid finance charges not retained by the creditor, a mortgage broker, or an affiliate of either.[20]

The new rate triggers for both "high-cost mortgages" and "higher-risk mortgages" under the Dodd-Frank Act are based on the percentage by which the APR exceeds APOR. Given this similarity, the Agencies sought comment in the higher-risk mortgage proposal on whether a modification should be considered for this final rule as well and, if so, what type of modification.

[17] *See* 2012 TILA-RESPA Proposal, 77 Fed. Reg. 51116, 51143-46, 51277-79, 51291-93, 51310-11 (Aug. 23, 2012).
[18] *See* 2012 HOEPA Proposal, 77 Fed. Reg. 49090, 49100-07, 49133-35 (Aug. 15, 2012).
[19] 15 U.S.C. 1639d; 76 FR 11598 (March 2, 2011).
[20] S*ee* 75 FR 58539, 58660-62 (Sept. 24, 2010); 76 FR 11598, 11609, 11620, 11626 (March 2, 2011).

Accordingly, the proposal defined "higher-risk mortgage loan" (termed HPML in this final rule) in the alternative as calculated by either the TCR or APR, with comment sought on both approaches. The Agencies relied on their exemption authority under section 1471 of the Dodd-Frank Act to propose this alternative definition of higher-risk mortgage. TILA section 129H(b)(4)(B), 15 U.S.C. 1639h(b)(4)(B).

On September 6, 2012, the Bureau published notice in the Federal Register that the comment period for public comments on the more inclusive definition of "finance charge" in the 2012 TILA-RESPA Proposal and the use of the TCR in the 2012 HOEPA Proposal would be extended to November 6, 2012.[21] The Bureau explained that it believed that commenters needed additional time to evaluate the proposed more inclusive finance charge in light of the other proposals affected by the more inclusive finance charge proposal and the Bureau's request for data on the effects of a more inclusive finance charge. The Bureau stated that it did not expect to address any proposed changes to the definition of finance charge or methods of reconciling an expanded definition of finance charge with APR coverage tests until it finalizes the disclosures in the 2012 TILA-RESPA Proposal. A final TILA-RESPA disclosure rule is not expected to be issued until sometime after January of 2013.

For this reason, this final rule requires creditors to determine whether a loan is an HPML by comparing the APR to the APOR and is not at this time finalizing the proposed alternative of replacing the APR with the TCR and comparing the TCR to the APOR. The Agencies will consider the merits of any modifications to this approach that might be necessary and public comments on this matter if and when the Bureau adopts the more inclusive definition of finance charge proposed in the 2012 TILA-RESPA Proposal.

[21] 77 FR 54843 (Sept. 6, 2012); 77 FR 54844 (Sept. 6, 2012).

Existing Definition of HPML versus New Definition of HPML

The new definition of HPML differs from the definition of HPML in existing § 1026.35(a)(1) in several respects.

First, the new definition of HPML incorporates an additional rate threshold for determining coverage for first-lien loans – an APR trigger of 2.5 percentage points above APOR for first-lien jumbo mortgage loans. The definition retains the APR triggers of 1.5 percentage points above APOR for first-lien conforming mortgages and 3.5 percentage points above APOR for subordinate-lien loans.

By statute, this additional APR threshold of 2.5 percentage points above APOR applies in determining coverage of both the escrow requirements in revised § 1026.35(b) and the appraisal requirements in revised § 1026.35(c). *See* TILA section 129D(b)(3)(B), 15 U.S.C. 1639d(b)(3)(B) (escrow rules); TILA section 129H(f)(2)(B), 15 U.S.C. 1639h(f)(2)(B) (appraisal rules). The APR trigger for first-lien jumbo loans has applied to the requirement to establish escrow accounts for HPMLs under Regulation Z since April 1, 2011. *See* existing § 1026.35(b)(3)(i) and (v); 76 FR 11319 (March 2, 2011).

Under the existing HPML rules in § 1026.35, the APR threshold of 2.5 percentage points above APOR applies only to the requirement to escrow HPMLs in § 1026.35(b)(3). *See* § 1026.35(b)(3)(v). Due to amendments to TILA mandated by the Dodd-Frank Act, however, existing HPML rules on repayment ability (§ 1026.35(b)(1)) and prepayment penalties (§ 1026.35(b)(2)) will be eliminated from the HPML rules in § 1026.35. New rules on repayment ability and prepayment penalties are incorporated into the Bureau's 2013 ATR Final Rule and final rules on "high-cost" mortgages. *See* § 1026.32(b)(6) and (d)(6), § 1026.43(b)(10), (c), (e).

Thus, as revised, § 1026.35 will have only two sets of rules for HPMLs – the escrow requirements in revised § 1026.35(b) and the appraisal requirements in new § 1026.35(c). The APR test of 2.5 percentage points above APOR applies, as noted, to both sets of rules, so is now folded into the general definition of HPML in § 1026.35(a)(1). Accordingly, the definition of "jumbo" loans in preexisting § 1026.35(b)(3)(v) is being removed.

A second change is that the revised HPML definition adds the qualification that an HPML is a "closed-end" consumer credit transaction. This change is not substantive; instead, it merely replaces text previously in § 1026.35(a)(3), that excludes from the definition of HPML "a home-equity line of credit subject to section 1026.5b." Other exemptions from the current definition of HPML listed in existing § 1026.35(a)(3) are moved into the specific provisions setting forth exemptions for certain types of HPMLs from coverage of the escrow rules and appraisal rules, respectively. *See* section-by-section analysis of § 1026.35(c)(2). Thus, the final rule eliminates § 1026.35(a)(3), but with no substantive change intended.

Third, with no substantive change intended, the language used to describe the HPML rate triggers has been revised from preexisting § 1026.35(a)(1) to conform to the language used in the proposed "higher-risk mortgage" appraisal rule, which in turn conforms more closely to the statutory language used to describe the rate triggers for "higher-risk mortgages" and similar statutory rate triggers for application of the escrow requirements. *See* TILA section 129D(B)(3), 15 U.S.C. 1639d(b)(3) (escrow rules); TILA section 129H(f)(2), 15 U.S.C. 1639h(f)(2) (appraisal rules).

Finally, the Official Staff Interpretations are reorganized with no substantive change intended. Specifically, comments 35(a)(2)-1 and -3, clarifying the terms "comparable transaction" and "rate set," respectively, are moved to comments 35(a)(1)-1 and 35(a)(1)-2. This modification reflects that the terms “comparable transaction” and “rate set” occur in the definition of “higher-priced mortgage loan” in § 1026.35(a)(1).

Comparable Transaction

As comment 35(a)(1)-1 indicates, the table of APORs published by the Bureau will provide guidance to creditors in determining how to use the table to identify which APOR is applicable to a particular mortgage transaction. The Bureau publishes on the internet, currently at http://www.ffiec.gov/ratespread/newcalc.aspx, in table form, APORs for a wide variety of mortgage transaction types based on available information. For example, the Bureau publishes a separate APOR for at least two types of variable rate transactions and at least two types of non-variable rate transactions. APORs are estimated APRs derived by the Bureau from average interest rates, points, and other loan pricing terms currently offered to consumers by a representative sample of creditors for mortgage transactions that have low-risk credit characteristics. Currently, the Bureau calculates APORs consistent with Regulation Z (*see* 12 CFR § 1026.22 *and* appendix J to part 1026), for each transaction type for which pricing terms are available from a survey, and estimates APORs for other types of transactions for which direct survey data are not available based on the loan pricing terms available in the survey and other information. However, data are not available for some types of mortgage transactions, including reverse mortgages. In addition, the Bureau publishes on the internet the methodology it uses to arrive at these estimates.

Rate Set

Comment 35(a)(1)-2 clarifies that a transaction’s APR is compared to the APOR as of the date the transaction's interest rate is set (or “locked”) before consummation. The comment notes that sometimes a creditor sets the interest rate initially and then re-sets it at a different level before consummation. Accordingly, under the final rule, for purposes of § 1026.35(a)(1), the creditor should use the last date the interest rate for the mortgage is set before consummation.

Average Prime Offer Rate

The Agencies are not separately publishing the definition of the term "average prime offer rate" in § 1026.35(a)(2). The meaning of this term is determined by the Bureau and is published and explained in the Bureau's 2013 Escrows Final Rule. Consistent with the proposal, in the Board's publication of this final rule, the term APOR is defined to have the same meaning as in § 1026.35(a)(2). *See* 12 CFR 226.43(a)(3)(Board). The OCC's publication of this final rule cross-references the definition of HPML, which incorporates the term APOR as defined in § 1026.35(a)(2). S*ee* 12 CFR 34.202(b). The OCC's and the Board's versions of Official Staff Interpretations to the final rule cross-reference comments to § 1026.35(a)(2) that explain the meaning of average prime offer rate as described below. *See* 12 CFR 34.202, comment 1 (OCC); 12 CFR 226.43, comment 2. Comment 35(a)(2)-1 clarifies that APORs are APRs derived from average interest rates, points, and other loan pricing terms currently offered to consumers by a representative sample of creditors for mortgage transactions that have low-risk pricing characteristics. Other pricing terms include commonly used indices, margins, and initial fixed-rate periods for variable-rate transactions. Relevant pricing characteristics include a consumer's credit history and transaction characteristics such as the loan-to-value ratio, owner-occupant status, and purpose of the transaction. Currently, to obtain APORs, the Bureau uses a survey of creditors that both meets the criteria of § 1026.35(a)(2) and provides pricing terms for at least two types of variable rate transactions and at least two types of non-variable rate transactions. The Freddie Mac Primary Mortgage Market Survey® is an example of such a survey, and is the survey currently used to calculate APORs.

Principal Dwelling

As in the proposal, the final versions of the OCC's and the Board's publication of the definition of "higher-priced mortgage loan" rules cross-reference the Bureau's Regulation Z and Official Staff Interpretations for the meanings of "principal dwelling," "average prime offer rate," "comparable transaction," and "rate set." *See* 12 CFR 34.202, comments 1 (OCC); 12 CFR 226.43(a)(3), comments 1, 2, 3, and 4 (Board). The Regulation Z comments to which the OCC's and Board's rules cross-reference regarding the meaning of "average prime offer rate," "comparable transaction," and "rate set" are described above. *See* 12 CFR 34.202, comment1 (OCC); 12 CFR 226.43(a)(3), comments 2, 3, and 4 (Board). A proposed comment cross-referencing the Bureau's Regulation Z for the meaning of the term "principal dwelling" is not adopted in the Bureau's version of the final rule because the meaning of "principal dwelling" in new § 1026.35(a)(1) is understood to be consistent within the Bureau's Regulation Z. The OCC's version of this final rule also does not include the proposed comment specifically cross-referencing the meaning of "principal dwelling" in the Bureau's Regulation Z because the OCC is adopting the Bureau's definition of HPML, which the Bureau's definition of "principal dwelling." *See* 12 CFR 34.202(b); *see also* 12 CFR 34.202, comment 1. The proposed comment is, however, adopted in the Board's publication of the rule. *See* 12 CFR 226.43(a)(3), comment 1. Consistent with the proposal, in the final rule, the term "principal dwelling" has the same meaning as in § 1026.2(a)(24) and is further explained in existing comment 2(a)(24)-3. Consistent with comment 2(a)(24)-3, a vacation home or other second home would not be a principal dwelling. However, if a consumer buys or builds a new dwelling that will become the consumer's principal dwelling within a year or upon the completion of construction, the comment clarifies that the new dwelling is considered the principal dwelling.

Threshold for "Jumbo" Loans

Comment 35(a)(1)-3 explains that § 1026.35(a)(1)(ii) provides a separate threshold for determining whether a transaction is a higher-priced mortgage loan subject to § 1026.35 when the principal balance exceeds the limit in effect as of the date the transaction's rate is set for the maximum principal obligation eligible for purchase by Freddie Mac (a "jumbo" loan). The comment further explains that FHFA establishes and adjusts the maximum principal obligation pursuant to rules under 12 U.S.C. 1454(a)(2) and other provisions of Federal law. The comment clarifies that adjustments to the maximum principal obligation made by FHFA apply in determining whether a mortgage loan is a "jumbo" loan to which the separate coverage threshold in § 1026.35(a)(1)(ii) applies.

The Board's publication of the definition of "higher-priced mortgage loan" rule in this final rule cross-references this comment in the Bureau's Official Staff Interpretations. *See* 12 CFR 226.43(a)(3), comment 3 (Board). The OCC's version of the final rule adopts this comment in 12 CFR 34.202, comment 1.

35(c) Appraisals for Higher-Priced Mortgage Loans

New § 1026.35(c) implements the substantive appraisal requirements for "higher-risk mortgages" in TILA section 129H. 15 U.S.C. 1639h. The OCC's and the Board's versions of these rules are substantively identical to the rules in § 1026.35(c). *See* 12 CFR 34.201 *et seq.* (OCC) and 12 CFR 226.43 (Board); s*ee also* section-by-section analysis of § 1026.35(c)(7).

35(c)(1) Definitions

As discussed above, revised § 1026.35(a) contains the definitions of HPML and APOR, which are used in both the HPML escrow rules in § 1026.35(b) and the HPML appraisal rules in new § 1026.35(c). Definitions specific to the substantive appraisal requirements of § 1026.35(c) are segregated in new § 1026.35(c)(1) and described below, along with applicable public comments.

35(c)(1)(i) Certified or Licensed Appraiser

TILA section 129H(b)(3) defines “certified or licensed appraiser” as a person who “(A) is, at a minimum, certified or licensed by the State in which the property to be appraised is located; and (B) performs each appraisal in conformity with the Uniform Standards of Professional Appraisal Practice and title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, and the regulations prescribed under such title, as in effect on the date of the appraisal.” 15 U.S.C. 1639h(b)(3). Consistent with the statute, the Agencies proposed to 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) (12 U.S.C. 3331 *et seq*.), and any implementing regulations in effect at the time the appraiser signs the appraiser’s certification.

The proposed definition of “certified or licensed appraiser” generally mirrors the statutory language in TILA section 129H(b)(3) regarding State licensing and certification. However, the Agencies proposed to use the defined term “State agency” to clarify that the appraiser must be certified or licensed by a State agency that meets the standards of FIRREA title XI. The proposal defined the term “State agency” to mean a “State appraiser certifying and licensing agency” recognized in accordance with section 1118(b) of FIRREA title XI (12 U.S.C.

3347(b)) and any implementing regulations.[22] *See* section-by-section analysis of § 1026.35(c)(1)(iv), below.

As discussed below, the Agencies are adopting the proposed definition of "certified or licensed appraiser" without change.

Uniform Standards of Professional Appraisal Practice (USPAP). Consistent with the statutory definition of "certified or licensed appraiser," the proposal incorporated into the proposed definition the requirement that, to be a "certified or licensed appraiser" under the appraisal rules, the appraiser has to perform the appraisal in conformity with the "Uniform Standards of Professional Appraisal Practice." A comment was proposed to clarify that USPAP refers to the professional appraisal standards established by the Appraisal Standards Board of the "Appraisal Foundation," as defined in FIRREA section 1121(9). 12 U.S.C. 3350(9). The Agencies believe that this terminology is appropriate for consistency with the existing definition in FIRREA title XI and adopt the definition and comment as proposed. *See* § 1026.35(c)(1)(i) and comment 35(c)(1)(i)-1.

In addition, TILA section 129H(b)(3) requires that the appraisal be performed in conformity with USPAP "as in effect on the date of the appraisal." 15 U.S.C. 1639h(b)(3). The Agencies proposed to incorporate this concept in the definition of "certified or licensed appraiser" and to include a comment clarifying that the "date of the appraisal" is the date on which the appraiser signs the appraiser's certification. Again, the Agencies adopt the definition

[22] If the Appraisal Subcommittee of the Federal Financial Institutions Examination Council issues certain written findings concerning, among other things, a State agency's failure to recognize and enforce FIRREA title XI standards, appraiser certifications and licenses issued by that State are not recognized for purposes of title XI and appraisals performed by appraisers certified or licensed by that State are not acceptable for federally-related transactions. 12 U.S.C. 3347(b).

and comment as proposed. *See* § 1026.35(c)(1)(i) and comment 35(c)(1)(i)-1. Thus, the relevant edition of USPAP is the one in effect at the time the appraiser signs the appraiser's certification.

Appraiser's certification. The proposal also included a comment to clarify that the term "appraiser's certification" refers to the certification that must be signed by the appraiser for each appraisal assignment as specified in USPAP Standards Rule 2-3.[23] The final rule adopts this clarification without change. *See* comment 35(c)(1)(i)-2.

FIRREA title XI and implementing regulations. As noted, TILA section 129H(b)(3) defines ''certified or licensed appraiser'' as a person who is certified or licensed as an appraiser and ''performs each appraisal in accordance with [USPAP] and title XI of [FIRREA], and the regulations prescribed under such title, as in effect on the date of the appraisal.'' 15 U.S.C. 1639h(b)(3). Section 1110 of FIRREA directs each Federal financial institutions regulatory agency[24] to prescribe "appropriate standards for the performance of real estate appraisals in connection with federally related transactions under the jurisdiction of each such agency or instrumentality." 12 U.S.C. 3339. These rules must require, at a minimum—(1) that real estate appraisals be performed in accordance with generally accepted appraisal standards as evidenced by the appraisal standards promulgated by the Appraisal Standards Board of the Appraisal Foundation; and (2) that such appraisals shall be written appraisals. 12 U.S.C. 3339(1) and (2).

The Dodd-Frank Act added a third requirement—that real estate appraisals be subject to appropriate review for compliance with USPAP—for which the Federal financial institutions regulatory agencies must prescribe implementing regulations. FIRREA section 1110(3), 12 U.S.C. 3339(3). FIRREA section 1110 also provides that each Federal banking agency may

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[23] *See* Appraisal Standards Bd., Appraisal Fdn., Standards Rule 2-3, USPAP (2012-2013 ed.) at U-29, *available at* http://www.uspap.org.
[24] The Federal financial institutions regulatory agencies are the Board, the FDIC, the OCC, and the NCUA.

require compliance with additional standards if the agency determines in writing that additional standards are required to properly carry out its statutory responsibilities. 12 U.S.C. 3339. Accordingly, the Federal financial institutions regulatory agencies have prescribed appraisal regulations implementing FIRREA title XI that set forth, among other requirements, minimum standards for the performance of real estate appraisals in connection with "federally related transactions," which are defined as real estate-related financial transactions that a Federal banking agency engages in, contracts for, or regulates, and that require the services of an appraiser.[25] 12 U.S.C. 3339, 3350(4).

The Agencies' proposal provided that the relevant provisions of FIRREA title XI and its implementing regulations are those selected portions of FIRREA title XI requirements ''applicable to appraisers,'' in effect at the time the appraiser signs the appraiser's certification. While the Federal financial institutions regulatory agencies' requirements in FIRREA also apply to an institution's ordering and review of an appraisal, the Agencies proposed that the definition of ''certified or licensed appraiser'' incorporate only FIRREA title XI's minimum standards related to the appraiser's performance of the appraisal. Accordingly, a proposed comment clarified that the relevant standards ''applicable to appraisers'' are found in regulations prescribed under FIRREA section 1110 (12 U.S.C. 3339) "that relate to an appraiser's development and reporting of the appraisal," and that paragraph (3) of FIRREA, which relates to the review of appraisals, is not relevant. The Agencies are adopting these proposals as § 1026.35(c)(1)(i) and comment 35(c)(1)(i)-3.

The Agencies also noted that FIRREA title XI applies by its terms to ''federally related transactions'' involving a narrower category of loans and institutions than the group of loans and

[25] *See* OCC: 12 CFR Part 34, Subpart C; Board: 12 CFR part 208, subpart E, and 12 CFR part 225, subpart G; FDIC: 12 CFR part 323; and NCUA: 12 CFR part 722.

lenders that fall within TILA's definition of "creditor."[26] For example, the FIRREA title XI regulations do not apply to transactions of $250,000 or less.[27] They also do not apply to non-depository institutions.[28] However, the Agencies believe that Congress, by including the higher-risk mortgage appraisal rules in TILA, which applies to all creditors, demonstrated its intention that all creditors that extend higher-risk mortgage loans, such as independent mortgage companies, should obtain appraisals from appraisers who conform to the standards in FIRREA related to the development and reporting of the appraisal. The Agencies also believe that, by placing this rule in TILA, Congress did not intend to limit its application to loans over $250,000. The Agencies adopt this broader interpretation in the final rule.

In the proposed rule, the Agencies did not identify specific FIRREA regulations that relate to the appraiser's development and reporting of the appraisal. The Agencies requested comment on whether the final rule should address any particular FIRREA requirements applicable to appraisers that related to the development and reporting of the appraisal. Consistent with the proposal, the final rule does not identify specific FIRREA regulations that relate to the appraiser's development and reporting of the appraisal.

Public Comments on the Proposal

Appraiser trade associations, a housing advocate, and a credit union commenter agreed that the rule should apply to all qualifying mortgage loans, and not only the subset of the higher-risk mortgage loans already covered by FIRREA, including those loans with a transaction value of $250,000 or less. The appraiser trade associations and the housing advocate commenters

[26] TILA section 103(g), 15 U.S.C. 1602(g) (implemented by § 1026.2(a)(17)). *See also* 12 U.S.C. 3350(4) and OCC: 12 CFR 34.42(f); Board: 12 CFR 225.62(f); FDIC: 12 CFR 323.2(f); and NCUA: 12 CFR 722.2(e) (defining "federally related transaction").
[27] *See* OCC: 12 CFR 34.43(a)(1); Board: 12 CFR 225.63(a)(1); FDIC: 12 CFR 323.3(a)(1); and NCUA: 12 CFR 722.3(a)(1).
[28] *See* 12 U.S.C. 3339, 3350(4) (defining "federally related transaction," (6) (defining "federal financial institutions regulatory agencies") and (7) (defining "financial institution").

believed that all higher-risk mortgages must be included in the rule to ensure that consumers receive the protections offered by appraisals. The housing advocate commenter also believed that including all higher-risk mortgages would reduce risk to all parties involved in the financing and servicing of mortgages and would ensure equal access to credit. This commenter specifically requested that the Agencies at least require an interior appraisal by licensed appraisers for all residential mortgages above $50,000, regardless of whether they are originated or insured by the private sector, Fannie Mae, Freddie Mac, or the Federal Housing Administration (FHA).

A banking trade association and a credit union commenter, however, believed that Congress intended the FIRREA requirements to apply only to a subset of higher-risk mortgages that are already covered by FIRREA. The banking trade association commenter believed the Agencies should not require the rule to apply to loans held in portfolio or loans with a value of $250,000 or less, because a bank holding a loan in portfolio has strong incentive to ensure that the property sale is legitimate and the property is properly valued. The commenter also believed the statute intended to apply the rules only to the subset of higher-risk mortgages with a value of over $250,000, as is provided in the Federal financial institutions regulatory agencies' regulations implementing FIRREA. The banking trade association and a bank commenter noted that many community banks, particularly in rural areas, limit costs to consumers by not requiring appraisals on mortgages held in portfolio of $250,000 or less as permitted under FIRREA title XI or by performing cheaper, in-house evaluations of property.

On whether the final rule should identify specific FIRREA regulations that relate to the development and reporting of the appraisal, the Agencies received one comment letter from appraiser trade associations. These commenters requested that the Agencies specify that creditors must use certified rather than licensed appraisers. The comment is discussed in more detail in the discussion of the use of “certified” versus “licensed” appraisers, below.

Discussion

As discussed in the proposal, the Agencies believe that, by referencing FIRREA requirements in the context of defining “certified or licensed appraiser,” the statute intended to limit FIRREA’s requirements to those that apply to the *appraiser’s* development and reporting of performance of the appraisal, rather than the FIRREA requirements that apply to a creditor’s ordering and review of the appraisal. TILA section 129H(b)(3), 15 U.S.C. 1639h(b)(3). The Agencies also did not propose to interpret ‘‘certified or licensed appraiser’’ to include requirements related to appraisal review under FIRREA section 1110(3) because these requirements relate to an institution’s responsibilities after receiving the appraisal, rather than to how the certified or licensed appraiser performs the appraisal. Comment 35(c)(1)(i)-3 is consistent with the proposal in this regard. Accordingly, as proposed, the final rule includes a comment clarifying that the requirements of FIRREA section 1110(3) that relate to the ‘‘appropriate review’’ of appraisals are not relevant for purposes of whether an appraiser is a certified or licensed appraiser under the proposal. *See* comment 35(c)(1)(i)-3.

At the same time and in light of public comments, the Agencies reviewed the relevant statutory provisions and confirmed their conclusion that applying the FIRREA requirements related to an appraiser’s performance of an appraisal broadly – to transactions originated by creditors and transaction types not necessarily subject to FIRREA (such as loans of $250,000 or less) – is wholly consistent with the consumer protection purpose of title XIV of the Dodd-Frank Act, as well as specific language of the appraisal provisions. For example, the Agencies believe that if Congress intended to limit application of the FIRREA requirements to mortgage loans covered by FIRREA, such as loans of over $250,000 made by Federally-regulated depositories, Congress would have expressly done so. Instead, Congress placed the appraisal requirements, including the definition of “certified and licensed appraiser” referencing FIRREA, in TILA, which applies to loans made by all types of creditors. Moreover, limiting coverage of the Dodd-Frank Act higher-risk mortgage appraisal rules to loans of over $250,000 would eliminate protections for most higher-risk mortgage consumers.[29] From a practical standpoint, the Agencies believe that the most reasonable interpretation of the statute is that all mortgage loans meeting the definition of “higher-risk mortgage” are subject to a uniform set of rules, regardless of the type of creditor. This creates a level playing field and ensures the same protections for all consumers of “higher-risk mortgages.” For these reasons, consistent with the proposal, the final rule applies the FIRREA requirements to appraisals for all HPMLs that are not exempt from the regulation. *See* § 1026.35(c)(2).

“Certified” versus “licensed” appraiser. Neither TILA section 129H nor the proposed rule defined the individual terms ‘‘certified appraiser’’ and ‘‘licensed appraiser,’’ or specified when a certified appraiser or a licensed appraiser must be used. Instead, the proposed rule required that creditors obtain an appraisal performed by ‘‘a certified or licensed appraiser.’’ 15 U.S.C. 1639h(b)(1), (b)(2). The Agencies noted in the proposal that certified appraisers generally differ from licensed appraisers based on the examination, education, and experience requirements necessary to obtain each credential. The proposal also stated that existing State and Federal law and regulations require the use of a certified appraiser rather than a licensed

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[29] According to HMDA data, mean loan size for purchase-money HPMLs in 2011 was $141,600 (median $109,000) and for refinance HPMLs in 2011, mean loans size was $141,600 (median $104,000). In 2010, mean loan size for purchase-money HPMLs was $140,400 (median $100,000) and for refinance HPMLs, mean loan size was $138,600 (median $95,000). *See* Robert B. Avery, Neil Bhutta, Kenneth B. Brevoort, and Glenn Canner, “The Mortgage Market in 2011: Highlights from the Data Reported under the Home Mortgage Disclosure Act,” FR Bulletin, Vol. 98, no. 6 (Dec. 2012) http://www.federalreserve.gov/pubs/bulletin/2012/PDF/2011_HMDA.pdf.

appraiser for certain types of transactions. The Agencies requested comment on whether the final rule should address the issue of when a creditor must use a certified appraiser rather than a licensed appraiser.

Consistent with the proposal, the final rule does not separately define “certified” appraiser or “licensed” appraiser, or specify when a creditor should use a “certified” rather than a “licensed” appraiser.

Public Comments on the Proposal

Several national and State credit union trade associations believed that the Agencies should not specify when a creditor must use a certified appraiser rather than a licensed appraiser and requested that the Agencies provide creditors with flexibility to make that determination. Some of these commenters noted that State requirements for certified or licensed appraisers may vary significantly; some states may not issue licenses for appraisers, and some may issue different certified appraiser credentials based on the type of property. A financial holding company commenter, on the other hand, requested that the Agencies clarify circumstances under which a lender must use a certified or a licensed appraiser to facilitate compliance.

On the other hand, appraiser trade association commenters believed that creditors should be required to use only certified appraisers, because the certification is more rigorous than licensure. These commenters stated that the FHA requires newly-eligible appraisers to be certified, and noted that many states have phased out, or are in the process of phasing out, the licensing of appraisers rather than certification. The commenters further stated that when collateral property is complex, the Agencies should require a certified appraiser who is also credentialed by a recognized professional appraisal organization. Similarly, a realtor trade association commenter believed that using certified appraisers was preferable. The commenter believed that the rule should define appraisals for higher-risk mortgages as "complex," thus requiring that only certified appraisers may perform the appraisals.

Discussion

As noted above, several commenters confirmed the Agencies' concerns that State requirements for certified or licensed appraisers may vary significantly and are evolving. Overall, the Agencies believe that imposing specific requirements in this rule about when a certified or licensed appraiser is required goes beyond the scope of the statutory "higher-risk mortgage" appraisal provisions in TILA section 129h. 15 U.S.C. 1639h. The Agencies do not believe that this rule is an appropriate vehicle for guidance on standards for use of a State certified or licensed appraiser that may change over time and vary by jurisdiction. Although the FIRREA appraisal regulations specifically require a "certified" appraiser for certain types of mortgage transactions, the Agencies do not believe that these FIRREA rules are incorporated into the higher-risk mortgage appraisal rules applicable to all creditors. *See* section-by-section analysis of § 1026.35(c)(1)(i) (defining "certified or licensed appraiser" to incorporate FIRREA requirements related to the development and reporting of the appraisal, not appraiser selection or review). Thus, the final rule need not clarify these rules for entities not subject to the FIRREA appraisal regulations; entities subject to the FIRREA appraisal regulations are familiar with them.

Appraiser competency. In the proposed rule, the Agencies also noted that, in selecting an appraiser for a particular appraisal assignment, creditors typically consider an appraiser's experience, knowledge, and educational background to determine the individual's competency to appraise a particular property and in a particular market. The proposed rule did not specify competency standards, but the Agencies requested comment on whether the rule should address appraiser competency. In keeping with the proposal, the final rule does not specify competency standards for appraisers.

Public Comments on the Proposal

A realtor trade association commenter suggested that the rule incorporate guidance from the Interagency Appraisal and Evaluation Guidelines[30] regarding creditors' criteria for selecting, evaluating, and monitoring the performance of appraisers. However, a banking trade association, a financial holding company, appraiser trade association, and several national and State credit union trade association commenters stated that the Agencies should not require creditors to apply specific competency standards for appraisers. Several commenters asserted that competency standards would result in increased regulatory burden and cost, and a banking trade association expressed concern that requiring creditors to implement subjective competency standards could raise conflict of interest issues with respect to appraiser independence.

Appraiser trade association commenters suggested that instead of setting forth competency standards, the Agencies should require a creditor to ensure that the engagement letter properly lays out the required scope of work, that the appraiser is independent, and that the appraiser possesses the appropriate experience to perform the assignment including, when necessary, geographic competency. The financial holding company commenter suggested that the rule should reference FIRREA and require creditors to ensure that appraisers are in good standing. The banking trade association commenter believed that the Agencies should include a reference to USPAP to create a uniform competency standard. One State credit union association believed that the Agencies should permit creditors to rely on appraisers' representations regarding licensing and certification.

[30] 75 FR 77450, 77465–68 (Dec. 10, 2010).

Discussion

The Agencies believe that the many aspects of appraiser competency are beyond the scope of TILA's "higher-risk mortgage" provisions defining "certified or licensed appraiser," which do not mention competency. Appraiser competency is addressed in a number of regulations and guidelines for Federally-regulated depositories, which are expected to know and follow rules and guidance under FIRREA regarding appraiser competency. [31]

35(c)(1)(ii) Manufactured Home

As discussed in in the section-by-section analysis of § 1026.35(c)(2)(ii), below, the final rule exempts a transaction secured by a new manufactured home from the appraisal requirements of § 1026.35(c). Accordingly, § 1026.35(c)(1)(ii) adds a definition of manufactured home, clarifying that, for the purposes of this section, the term manufactured home has the same meaning as in HUD regulation 24 CFR 3280.2.

35(c)(1)(iii) National Registry

As discussed in § 1026.35(c)(3)(ii)(B) below, to qualify for the safe harbor provided in the final rule, a creditor must verify through the ''National Registry'' that the appraiser is a certified or licensed appraiser in the State in which the property is located as of the date the appraiser signs the appraiser's certification. Under FIRREA section 1109, the Appraisal Subcommittee of the FFIEC is required to maintain a registry of State certified and licensed appraisers eligible to perform appraisals in connection with federally related transactions. 12 U.S.C. 3338. For purposes of qualifying for the safe harbor, the final rule requires that a creditor must verify that the appraiser holds a valid appraisal license or certification through the registry

[31] *See, e.g.*, *id.* at 77465–68 (Dec. 10, 2010). Appraiser competency is critical to the quality and accuracy of residential mortgage appraisals. As a commenter noted, the federal banking agencies provide guidance in the Interagency Appraisal and Evaluation Guidelines regarding creditors' criteria for selecting, evaluating, and monitoring the performance of appraisers. *See id.*

maintained by the Appraisal Subcommittee. Thus, as proposed, § 1026.35(c)(1)(iii) in the final rule provides that the term ''National Registry'' means the database of information about State certified and licensed appraisers maintained by the Appraisal Subcommittee of the FFIEC.

35(c)(1)(iv) State Agency

TILA section 129H(b)(3)(A) provides that, among other things, a certified or licensed appraiser means a person who is certified or licensed by the ''State'' in which the property to be appraised is located. 15 U.S.C. 1639h(b)(3)(A). As discussed above, a certified or licensed appraiser means a person certified or licensed by the ''State agency'' in the State in which the property that secures the transaction is located. Under FIRREA section 1118, the Appraisal Subcommittee of the FFIEC is responsible for recognizing each State's appraiser certifying and licensing agency for the purpose of determining whether the agency is in compliance with the appraiser certifying and licensing requirements of FIRREA title XI. 12 U.S.C. 3347. In addition, FIRREA section 1120(a) prohibits a financial institution from obtaining an appraisal from a person the financial institution knows is not a State certified or licensed appraiser in connection with a federally related transaction. 12 U.S.C. 3349(a). Accordingly, as proposed, § 1026.35(c)(1)(iv) in the final rule defines the term ''State agency'' as a ''State appraiser certifying and licensing agency'' recognized in accordance with section 1118(b) of FIRREA and any implementing regulations.

35(c)(2) Exemptions

The Agencies proposed to exclude from the definition of "higher-risk mortgage loan," and thus from coverage of TILA's "higher-risk mortgage" appraisal rules entirely, the following types of loans: (1) qualified mortgage loans as defined in § 1026.43(e); (2) reverse-mortgage transactions subject to § 1026.33(a); and (3) loans secured solely by a residential structure.

These exclusions were proposed consistent with the express language of TILA section 129H(f) and pursuant to the Agencies' exemption authority in TILA section 129H(b)(4)(B), which authorizes the Agencies to exempt from coverage of the appraisal rules a class of loans if the Agencies determine that the exemption is in the public interest and promotes the safety and soundness of creditors. 15 U.S.C. 1639h(b)(4)(B) and (f).

The Agencies requested comment on these proposed exemptions. In addition, the Agencies requested comment on whether the final rule should exempt the following types of loans:

- Loans to finance new construction of a dwelling;
- Temporary or "bridge" loans, typically used to purchase a new dwelling where the consumer plans to sell the consumer's current dwelling; and
- Loans secured by properties in "rural" areas. For this last exemption, the Agencies requested comment on how to define "rural"; specifically, whether to define it as the Board did in its proposal to implement Dodd-Frank Act ability-to-repay requirements under TILA section 129C. *See* 15 U.S.C. 1639c; 76 FR 27390 (May 11, 2011) (2011 ATR Proposal) (and also in the 2011 Escrows Proposal), discussed in more detail below.

Finally, the Agencies requested comment on whether commenters believed that any other types of loans should be exempt from the final rule.

The final rule adopts two of the proposed exemptions: qualified mortgages and reverse mortgages. *See* § 1026.35(c)(2)(i) and (vi). The final rule also adopts exemptions for loans secured by new manufactured homes and by mobile homes, boats, or trailers, which replace the proposed exemption for loans secured solely by a residential structure. *See* § 1026.35(c)(2)(ii) (new manufactured homes) and (iii) (mobile homes, boats, or trailers). In addition, the final rule exempts the two types of loans on which the Agencies specifically requested comment: new construction loans and bridge loans. *See* § 1026.35(c)(2)(iv) (construction loans) and (v) (bridge loans).

In addition, based on public comments, the Agencies intend to publish a supplemental proposal to request comment on possible exemptions for "streamlined" refinance programs and small dollar loans, as well as to seek comment on whether application of the HPML appraisal rule to loans secured by certain other property types, such as existing manufactured homes, is appropriate.

Exemptions from the HPML appraisal rules of § 1026.35(c) are set out in new § 1026.35(c)(2). The structure of the final rule differs from that of the proposed rule. The proposed rule excluded certain loan types from the definition of "higher-risk mortgage loan" and thereby excluded these loan types from coverage of all of the "higher-risk mortgage" appraisal rules. By contrast, the final rule defines a general term – HPML – and incorporates exemptions from the appraisal rules in a separate subsection, § 1026.35(c)(2). As discussed, the general term HPML applies also to loans covered by the revised escrow rules in § 1026.35(b), with exemptions specific to those rules enumerated separately in § 1026.35(b)(2).

Thus, exemptions that are the same in both the escrow rules in § 1026.35(b) and the appraisal rules in § 1026.35(c) are stated separately in the "exemptions" sections for each set of rules. *See* § 1026.35(b)(2) and (c)(2). The following exemptions are generally the same for both the HPML escrow rules and the HPML appraisal rules: new construction loans, bridge loans, and reverse mortgages. The intent of this structure is to make clear that the Agencies jointly have authority to exempt transactions from the appraisal rules, whereas only the Bureau has authority to exempt transactions from the escrow rules.

These exemptions and related public comments are discussed in detail below.

35(c)(2)(i)

Qualified Mortgages

TILA section 129H(f) expressly excludes from the definition of higher-risk mortgage any loan that is a qualified mortgage as defined in TILA section 129C and a reverse mortgage loan that is a qualified mortgage as defined in TILA section 129C. 15 U.S.C. 1639(f). Rather than implement one exclusion for qualified mortgages and a separate exclusion for any reverse mortgage loans that may be defined by the Bureau as qualified mortgages, the Agencies proposed to provide a single exclusion for a qualified mortgage as that term would be defined in the Bureau's final rule implementing TILA section 129C. 15 U.S.C. 1639c.

Before authority regarding TILA section 129C transferred to the Bureau under the Dodd-Frank Act, the Board issued the 2011 ATR Proposal, which, among other things, would have defined a "qualified mortgage" in a new subsection of Regulation Z. 12 CFR 226.43(e). *See* 76 FR 27390, 27484-85 (May 11, 2011). During the proposal period for the "higher-risk mortgage" rule, the Bureau had not yet issued final rules implementing TILA section 129C's definition of "qualified mortgage." Since that time, the Bureau has issued rules defining "qualified mortgage." *See* 2013 ATR Final Rule, § 1026.43(e). Consistent with the proposed definition of "qualified mortgage," the Bureau's final rule defines "qualified mortgage" as generally including loans characterized by the absence of certain features considered risky, such as negative amortization and balloon payments.

The Agencies adopt the exemption for "qualified mortgages" as proposed, with a cross-reference to the Bureau's final rules defining this class of loans in 12 CFR 1026.43(e).

Public Comments on the Proposal

All commenters—including national and State credit union trade associations, as well as national and State banking trade associations—supported this exemption. Some banking trade associations believed the exemption was appropriate because qualified mortgages, by definition, are safe and sound transactions. Other banking and credit union trade associations expressed concern that they could not comment specifically on the exemption, because the term was not yet defined by the Bureau.

Discussion

The final rule incorporates the exemption for "qualified mortgages" as proposed because the exemption is prescribed by statute and widely supported by commenters. The Agencies note that some commenters requested that the final rule also exempt "qualified residential mortgages," which the Dodd-Frank Act exempts from the risk retention rules prescribed by the Act. *See* Dodd-Frank Act § 941, section 15G of the Securities Exchange Act of 1934, 15 U.S.C. 780-11(c)(1)(C)(iii). A qualified residential mortgage, however, is by statute to be defined by regulation as "no broader than" the definition of qualified mortgage prescribed by the Bureau in its 2013 ATR Final Rule. *See id.* at sec. 780-11(e)(4)(C). Therefore, the exemption for qualified mortgages will capture all qualified residential mortgages and a separate exemption is not necessary.

35(c)(2)(ii)

Transactions Secured by a New Manufactured Home

The Agencies proposed to exclude from coverage of the higher-risk mortgage appraisal rules any loan secured solely by a residential structure, such as a manufactured home.[32] The Agencies believed that requiring appraisals performed by certified or licensed appraisers was not appropriate, because such transactions typically more closely resemble titled vehicle loans. At the same time, based on outreach, the Agencies believed that for loans for residential structures, such as manufactured homes that are secured by both the home and the land to which the home is attached, appraisals performed by certified or licensed appraisers are feasible. Such transactions were therefore covered by the proposed rule. The Agencies believed the exemption for a loan secured solely by a residential structure was appropriate pursuant to the exemption authority under TILA section 129H(b)(4)(B). 15 U.S.C. § 1026.35(b)(4)(B).

The Agencies requested comment on whether the proposed exclusion was appropriate, and if not, reasonable methods by which creditors could comply with the requirements of this proposed rule when providing loans secured solely by a residential structure. The Agencies also requested comment on whether some alternative standards for valuing residential structures securing higher-risk mortgage loans might be feasible and appropriate to include as part of the final rule, in lieu of an appraisal performed by a certified or licensed appraiser.

Public Comments on the Proposal

Commenters, including national and State credit union trade associations, a manufactured housing industry consultant, manufactured housing trade associations, a realtor trade association, a lender specializing in manufactured housing financing, and national and State banking trade

[32] The Agencies proposed to exclude from the definition of "higher-risk mortgage loan" any loans secured solely by a "residential structure," as that term is used in Regulation Z's definition of "dwelling." *See* 12 CFR 1026.2(a)(19). The provision was intended to exclude loans that are not secured in whole or in part by land. Thus, for example, loans secured by manufactured homes that are not also secured by the land on which they are sited were proposed to be excluded from the definition of higher-risk mortgage loan, regardless of whether the manufactured home itself is deemed to be personal property or real property under applicable State law.

associations, submitted comments regarding the exemption for loans secured "solely by a residential structure," but limited their comments to the exemption as applied to manufactured homes. The commenters supported exempting loans secured solely by manufactured homes. Banking trade association commenters believed that the statute was intended to apply only to loans secured at least in part by real property. A manufactured housing industry consultant, a manufactured housing lender, and manufactured housing trade association commenters concurred that traditional appraisals were not appropriate for these transactions for a variety of reasons, including: (1) a lack of qualified and trained appraisers to appraise such transactions, especially in rural areas; (2) a lack of comparable sales and limited sales volume; (3) the high expense of appraisals relative to the cost of the transaction; and (4) inaccurate valuations resulting from traditional appraisals. The manufactured housing industry consultant suggested that an exemption was necessary in part because these loans were unlikely to qualify for the qualified mortgage exemption due to their small size, which would in turn increase the likelihood that they would exceed the points and fees thresholds defining qualified mortgages. *See* § 1026.43(e)(3).

Some of the commenters believed the Agencies should expand the exemption to include financing for both real estate and manufactured homes, known as "land home" financing. Manufactured housing trade association commenters argued that traditional appraisals are not appropriate for these transactions for many of the same reasons cited for excluding loans secured solely by a residential structure. One of these manufactured housing trade associations also expressed the view that appraisals are not appropriate because the cost of the home itself is readily known to consumers through other means. In addition, the commenter stated that in rural areas, the cost of the land is small compared to the overall value of the transaction.[33] This commenter recommended that if the Agencies did not exclude all land home transactions, the Agencies in the alternative should at least exclude those land home transactions that are under $125,000 or that are in a rural area.

One commenter also questioned the feasibility of appraisals for such transactions. A lender specializing in manufactured housing financing stated that, in land home transactions, the land on which manufactured homes will be located is often not identified until well after the time appraisals are typically ordered. Moreover, the commenter stated that manufactured homes are typically not available for an interior visit until after closing, regardless of whether the transaction is secured solely by the home itself or by land and home together. As an alternative, the commenter suggested different regulatory language for the exclusion, which would expand the exemption to land home transactions and would incorporate an existing definition of "manufactured home" to clearly eliminate site-built manufactured homes from the exemption.

Discussion

Public commenters generally confirmed Agencies' concerns regarding the application of the appraisal rules to loans secured by certain manufactured homes. Accordingly, the Agencies are excluding certain manufactured homes from coverage under the final rule. However, in the final rule, the Agencies are modifying the exemption. The proposed rule would have exempted loans "secured solely by a residential structure," which was intended to exempt manufactured homes and other types of dwellings when the loan was not secured at least in part by land. The language in the final rule is tailored to exempt transactions secured by specific types of

[33] Note, however, that another manufactured housing trade association commenter stated that the majority of manufactured homes are not considered an improvement or enhancement of the real property on which they are sited.

dwellings. Accordingly, the final rule exempts transactions secured by a new manufactured home, regardless of whether the structure is attached to land or considered real property, and also exempts transactions secured by a mobile home, boat, or trailer.

The Agencies believe that the manufactured home exemption should be based on whether the manufactured home securing the transaction is a new home, regardless of whether land also secures the transaction. Upon further consideration, the Agencies believe that TILA section 129H is intended to apply to certain transactions without regard to whether a transaction is secured by land.[34] Thus, the approach in the final rule is focused on the feasibility and utility of requiring certified or licensed appraisers to perform appraisals for particular manufactured home transactions.

The Agencies believe that an exemption for new manufactured homes regardless of whether the loan for such a home is also secured by land more precisely excludes from the rule those transactions that should not be subject to the new appraisal requirements. Based on further outreach, the Agencies understand that for loans secured by both new manufactured homes and land, a valuation is often performed by combining the manufactured home invoice price with the value of the land, rather than by a traditional appraisal that is based on the collective value of the structure and the land on which it is sited.

The Agencies believe that requiring traditional appraisals with interior inspections for transactions secured by a new manufactured home would add very little value to the consumer beyond existing valuation methods. Moreover, because it may be difficult or impossible to retain

[34] The Agencies note that the definition of "higher-risk mortgage loan" in TILA section 129H incorporates the definition of "residential mortgage loan." TILA section 129H(f). A residential mortgage loan is defined, in part, to include loans involving certain types of dwellings that are non-real estate residences. TILA section 103(cc)(5). For example, cooperatives are specifically described as dwellings under TILA section 103(w). Moreover, although TILA section 129H requires appraisals that conform to FIRREA title XI, the Agencies do not believe that TILA section 129H is limited to transactions subject to FIRREA title XI or other Federal regulations. Thus, the Agencies believe the statute intended to apply the appraisal requirements to some loans that are not secured by land.

qualified appraisers to perform such appraisals, the rule could result in some creditors declining to extend loans for manufactured homes. Exempting new manufactured homes from the rule is, therefore, in the public interest. The Agencies believe that such an exemption also promotes the safety and soundness of creditors, because creditors will be able to continue relying on standardized valuations that are more conducive to pricing new manufactured homes than are appraisals performed by a certified or licensed appraiser.

Accordingly, in § 1026.35(c)(2)(ii), the Agencies are exempting from the appraisal requirements of § 1026.35(c) a transaction secured by a new manufactured home. Comment 35(c)(2)(ii)-1 in the final rule clarifies that a transaction secured by a new manufactured home, regardless of whether the transaction is also secured by the land on which it is sited, is not a "higher-priced mortgage loan" subject to the appraisal requirements of § 1026.35(c).

35(c)(2)(iii)

Transaction Secured by Mobile Home, Boat, or Trailer

Section 1026.35(c)(2)(iii) of the final rule also specifically exempts transactions secured by a mobile home, boat, or trailer. This is consistent with the proposal, which would have exempted these transactions because they are secured "solely by a residential structure." The Agencies note that this exemption applies even if the transaction is also secured by land. Comment 35(c)(2)(iii)-1 clarifies that, for purposes of the exemption in § 1026.35(c)(2)(iii), a mobile home does not include a manufactured home, as defined in § 1026.35(c)(1)(ii).

The Agencies believe the exemption is in the public interest, because requiring an appraisal with an interior property visit for these transactions would offer limited value due to existing pricing tools, such as new product invoices and publicly-available pricing guides. The Agencies further believe, for purposes of safety and soundness, that creditors would be better served by using other valuation methods geared specifically for mobile homes, boats, and trailers.

35(c)(2)(iv)

Construction Loans

In the proposal, the Agencies asked for comment on whether to exempt from the higher-risk mortgage appraisal rules transactions that finance the construction of a new home. The Agencies recognized that for loans that finance the construction of a new home, an interior visit of the property securing the loan is generally not feasible because the homes are proposed to be built or are in the process of being built. At the same time, the Agencies recognized that construction loans that meet the pricing thresholds for higher-risk mortgage loans could pose many of the same risks to consumers as other types of loans meeting those thresholds. The Agencies therefore requested comment on whether to exclude construction loans from the definition of higher-risk mortgage loan. The Agencies also sought comment on whether, if an exemption for initial construction loans were not adopted in the final rule, creditors needed any additional compliance guidance for applying TILA's "higher-risk mortgage" appraisal rules to construction loans. Alternatively, the Agencies requested comment on whether construction loans should 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.

The final rule adopts an exemption from all of the HPML appraisal requirements for a "transaction that finances the initial construction of a dwelling." This exemption mirrors an existing exemption from the current HPML rules. *See* existing § 1026.35(a)(3), also retained in the 2013 Escrows Final Rule, § 1026.35(b)(2)(i)(B).

Public Comments on the Proposal

Appraiser trade association commenters believed that new construction loans should not be exempted because consumers needed the protection of the appraisal rules. However, all other commenters – including national and State credit union trade associations, national and State banking trade associations, banks, a mortgage company, a financial holding company, a home builder trade association, and a loan origination software company – supported the proposed exemption.

Commenters that supported an exemption for new construction loans had varying views on the risks associated with these loans, all supporting the commenters' request for an exemption for such loans. A loan origination software company and a bank commenter asserted that new construction loan interest rates and fees are often high because the loans, which are short-term, have inherently greater risk. Thus, the appraisal rules would be over-inclusive because they would apply even when extended to prime borrowers. Similarly, a banking association commenter argued that new construction loans are not those that Congress intended to target in the appraisal rules, which the commenter viewed as loans priced higher due to the relative credit risk of the borrower. The home builder trade association, however, supported an exemption because the commenter believed that new construction loans are not as risky as the loans targeted by Congress in the "higher-risk mortgage" appraisal rules because these loans require close coordination between a bank, home builder, and consumer.

The financial holding company, mortgage company, banking association, and loan origination software company commenters supported an exemption for new construction loans because they are temporary. One of these commenters noted that most mortgage-related regulations, such as those in Regulation X and Z, make accommodations for temporary loans. Others noted that the property securing the new construction loan ultimately will be subject to an appraisal under TILA's "higher-risk mortgage" appraisal rules if the permanent financing replacing the new construction loan is a "higher-risk mortgage."

Several commenters supporting an exemption cited concerns about the feasibility and utility of performing interior inspection appraisals during the construction phase. A bank commenter stated that an exemption was needed because a home under construction is not available for a physical inspection. Similarly, credit union association and banking association commenters stated that an interior visit would not be feasible during the construction phase. Moreover, the commenter believed an appraisal was unlikely to yield sufficient information about the condition of the property to justify the expense to the consumer. A banking association commenter further asserted that the usual value of a new construction loan is the value "at completion," so an appraisal performed during construction would not assess the value of a completed home.

A State banking association commenter asserted that failing to exempt new construction loans from the final rule would result in operational difficulties and that an interior inspection appraisal would be of little value to consumers in these circumstances. A bank commenter requested guidance on how to comply with the rules for these loans, if the Agencies did not exempt them from the rule.

Discussion

In § 1026.35(c)(2)(iv), the Agencies are using their exemption authority to exempt from the final rule a "transaction to finance the initial construction of a dwelling." Unlike the exemption for "bridge" loans that the Agencies are also adopting (*see* section-by-section analysis of § 1026.35(c)(2)(v), below), the exemption for new construction loans is not limited to loans of twelve months or less. This is because the Agencies recognize that new construction might take longer than twelve months and that therefore new construction loans might be for terms of longer than twelve months. This aspect of the exemption adopted in the final rule also reflects the existing exemption for new construction loans from the current HPML rules. *See* § 1026.35(a)(3).

The Agencies' decision to exempt these types of transactions is consistent with wide support for this exemption received from commenters, which largely confirmed the Agencies' concerns about the drawbacks of subjecting these transactions to the new HPML appraisal requirements, particularly the requirement for an interior inspection, USPAP-compliant appraisal. The Agencies also believe that this exemption is important to ensure consistency across mortgage rules, and thus to facilitate compliance. In addition to noting the existing exemption for new construction loans from the current HPML requirements, the Agencies also note the exemption for these loans from the new Dodd-Frank Act ability-to-repay and "high-cost" mortgage rules issued by the Bureau. *See* 2013 ATR Final Rule, § 1026.43(a)(3)(ii), and 2013 HOEPA Final Rule, § 1026.32(a)(2)(ii).[35]

Due to their temporary nature and for other reasons, these loans tend to have higher rates and thus more of them would be subject to the HPML appraisal rules without an exemption. Applying the HPML appraisal rules to these products might subject them to rules with which creditors might not in fact be able to comply. The Agencies therefore believe that this exemption will help ensure that a useful credit vehicle for consumers remains available to build and revitalize communities. The Agencies also recognize that new construction loans can be an important product for many creditors, enabling them to strengthen and diversify their lending portfolios. The Agencies are also not aware of, and commenters did not offer, evidence of

[35] Moreover, the existing "high-cost" mortgage rules contain a longstanding exemption for construction loans from the limitation on balloon payments. *See* existing § 1026.32(d)(1)(i).

widespread valuation abuses in loans to finance new construction. Thus, the Agencies find that the exemption is both in the public interest and promotes the safety and soundness of creditors. *See* TILA section 129H(b)(4)(B), 15 U.S.C. 1639h(b)(4)(B).

The Agencies also wished to clarify in the final rule the treatment of "construction to permanent" loans, consisting of a single loan that transforms into permanent financing at the end of the construction phase. For this reason, the commentary of the final rule includes guidance on the application of various rules in Regulation Z to these loans that parallels guidance provided in commentary for the new "high-cost" mortgage rules. *See* 2013 HOEPA Final Rule, comment 32(a)(2)(ii)-1. Specifically, comment 35(c)(2)(iv)-1 clarifies that the exclusion for loans to finance the initial construction of a dwelling applies to a construction-only loan as well as to the construction phase of a construction-to-permanent loan. The comment further clarifies that the HPML appraisal rules in § 1026.35(c) do apply if the permanent financing qualifies as an HPML under § 1026.35(a)(1) and is not otherwise exempt from the rules under § 1026.35(c)(2).

The comment also provides guidance on the application of Regulation Z's general closed-end mortgage loan disclosure requirements to construction-to-permanent loans. To this end, the comment states that, when a construction loan may be permanently financed by the same creditor, the general disclosure requirements for closed-end credit (§ 1026.17) provide that the creditor may give either one combined disclosure for both the construction financing and the permanent financing, or a separate set of disclosures for each of the two phases as though they were two separate transactions. *See* § 1026.17(c)(6)(ii) and comment 17(c)(6)-2. The comment explains that § 1026.17(c)(6)(ii) addresses only how a creditor may elect to disclose a construction-to-permanent transaction, and that which disclosure option a creditor elects under § 1026.17(c)(6)(ii) does not affect whether the permanent phase of the transaction is subject to

§ 1026.35(c). The comment further explains that, when the creditor discloses the two phases as separate transactions, the annual percentage rate for the permanent phase must be compared to the average prime offer rate for a transaction that is comparable to the permanent financing to determine coverage under § 1026.35(c). The comment also explains that, when the creditor discloses the two phases as a single transaction, a single annual percentage rate, reflecting the appropriate charges from both phases, must be calculated for the transaction in accordance with § 1026.35 and appendix D to part 1026. The comment also clarifies that the APR must be compared to the APOR for a transaction that is comparable to the permanent financing to determine coverage under § 1026.35(c). If the transaction is determined to be an HPML that is not otherwise exempt under § 1026.35(c)(2), only the permanent phase is subject to the HPML appraisal requirements of § 1026.35(c).

35(c)(2)(v)

Bridge Loans

In the proposal, the Agencies also requested comment on whether the appraisal rules of TILA section 129H should apply to temporary or "bridge" loans with a term of 12 months or less. 15 U.S.C. 1639h. If such an exemption were not adopted, the Agencies sought comment on whether any additional compliance guidance would be needed for applying the new appraisal rules to bridge loans. The Agencies stated concerns about the burden to both creditors and consumers of imposing the rule's requirements on such loans and questioned whether such requirements would be useful for many consumers.

As explained in the proposal, bridge loans are short-term loans typically used when a consumer is buying a new home before selling the consumer's existing home. Usually secured by the existing home, a bridge loan provides financing for the new home (often in the form of the down payment) or mortgage payment assistance until the consumer can sell the existing home and secure permanent financing. Bridge loans normally carry higher interest rates, points and fees than conventional mortgages, regardless of the consumer's creditworthiness.

In § 1026.35(c)(2)(v), the final rule adopts an exemption from the new HPML appraisal rules for a "loan with a maturity of 12 months or less, if the purpose of the loan is a 'bridge' loan connected with the acquisition of a dwelling intended to become the consumer's principal dwelling."

Public Comments on the Proposal

Almost all commenters—including national and State banking associations, national and State credit union associations, a mortgage company, a financial holding company, a loan origination software company, a home builder trade association, and a bank—supported an exemption for bridge loans for many of the same reasons that commenters supported exempting construction loans. Several commenters emphasized that these loans are temporary, and some further pointed out that imposing appraisal requirements was unnecessary because bridge loans are ultimately converted to permanent financing that will be subject to the appraisal rules. Other commenters argued that the protections of the appraisal rules were not needed because bridge loans' higher rates are generally unrelated to a consumer's creditworthiness; they argued that TILA's new "higher-risk mortgage" appraisal rules were intended for loans made to more vulnerable, less creditworthy consumers without other credit options.

Some commenters asserted that failing to exempt these loans would result in operational difficulties and would be of little value to consumers. In this regard, one commenter discussed the difficulties of comparing an APR to a "comparable" APOR for these loans. One credit union association commenter believed that without an exemption, consumers' access to bridge loans would be reduced. Some commenters requested that the Agencies exempt all types of temporary loans. Appraiser trade association commenters believed that the Agencies should not allow an exemption unless there was a compelling policy reason to do so.

Discussion

The Agencies are adopting an exemption for "bridge" loans of 12 months or less that are connected with the acquisition of a dwelling intended to become the consumer's principal dwelling for several reasons. First, the Agencies believe that with this exemption, the consumer would still be afforded the protection of the appraisal rules. This is because bridge loans used in connection with the acquisition of a new home are typically secured by the consumer's existing home to facilitate the purchase of a new home. Thus, the consumer would be afforded the protections of the appraisal rules on the permanent financing secured by the new home. This would include the protections of § 1026.35(c)(4)(i) regarding properties that are potentially fraudulent flips.

Second, commenters generally confirmed the Agencies' concerns expressed in the proposal about the burden to both creditors and consumers of imposing TILA section 129H's heightened appraisal requirements on short-term financing of this nature. As noted in the proposal, the Agencies recognize that rates on short-term bridge loans are often higher than on long-term home mortgages, so these loans may be more likely to meet the "higher-risk mortgage loan" triggers. As also noted in the proposal and echoed by commenters, "higher-risk mortgages" under TILA section 129H would generally be a credit option for less creditworthy consumers, who may be more vulnerable than others and in need of enhanced consumer protections, such as TILA section 129H's special appraisal requirements. However, a bridge loan consumer could be subject to rates that would exceed the higher-risk mortgage loan thresholds even if the consumer would qualify for a non-higher-risk mortgage loan when seeking permanent financing. The Agencies do not believe that Congress intended TILA section 129H to apply to loans simply because they have higher rates, regardless of the consumer's creditworthiness or the purpose of the loan.

Further, the Agencies recognize that the exemption can help facilitate compliance by generally ensuring consistency across residential mortgage rules. Such consistency can reduce compliance-related burdens and risks, thereby promoting the safety and soundness of creditors. The Agencies also believe that consistency across the rules can reduce operational risk and support a creditor's ability to offer these loans, which can enable creditors to strengthen and diversify their lending portfolios.

In particular, the Agencies note the current exemption for "temporary or 'bridge' loans of twelve months or less from the existing HPML rules (retained in the 2013 Escrows Final Rule, § 1026.35(b)(2)(i)(C)), but also a similar exemption from TILA's new ability-to-repay requirements. *See* existing § 1026.35(a)(3). *See* TILA section 129C(a)(8), 15 U.S.C. 1639c(a)(8); 2013 ATR Final Rule, § 1026.43(a)(3)(ii).[36] In addition, longstanding HOEPA rules have included an exception from the balloon payment prohibition for "loans with maturities of less than one year, if the purpose of the loan is a 'bridge' loan connected with the acquisition or construction of a dwelling intended to become the consumer's principal dwelling." § 1026.32(d)(1)(ii). The final HOEPA rules adopted by the Bureau contain the same exception with minor changes for conformity across mortgage rules. *See* 2013 HOEPA Final Rule,

[36] The exemption for "temporary or 'bridge' loans of twelve months or less" in TILA's ability-to-repay rules codifies an exemption from the current "high-cost" and HPML repayment ability requirements. *See* existing §§ 1026.34(a)(4)(v), 1026.35(a)(3) and (b)(1).

§ 1026.32(d)(1)(ii)(B) (revising the exception to cover bridge loans of 12 months or less, rather than less than one year).

Like the HOEPA exception from the balloon payment prohibition, the final HPML appraisal rule does not exempt all loans with terms of 12 months or less. Only bridge loans of 12 months or less that are made in connection with the acquisition of a consumer's principal dwelling are exempted. (Construction loans are separately exempted under § 1026.35(c)(2)(iv), discussed in the corresponding section-by-section analysis above.) The Agencies believe that the HPML appraisal rule might be appropriately applied to other types of temporary financing, particularly temporary financing that does not result in the consumer ultimately obtaining permanent financing covered by the appraisal rule.

Finally, as with new construction loans, the Agencies are not aware of, and commenters did not offer, evidence of widespread valuation abuses in bridge loans of twelve months or less used in connection with the acquisition of a consumer's principal dwelling. For all these reasons, the Agencies find that the exemption is both in the public interest and promotes the safety and soundness of creditors. *See* TILA section 129H(b)(4)(B), 15 U.S.C. 1639h(b)(4)(B).

35(c)(2)(vi)

Reverse Mortgage Transactions

The Agencies proposed to exempt reverse mortgage transactions subject to § 1026.33(a) from the definition of "higher-risk mortgage loan." The Agencies proposed this exemption in part because the proprietary (private) reverse mortgage market is effectively nonexistent, thus the vast majority of reverse mortgage transactions made in the United States today are insured by FHA as part of the U.S. Department of Housing and Urban Development's (HUD) Home Equity

Conversion Mortgage (HECM) Program.[37] The Agencies stated that TILA's new "higher-risk mortgage" appraisal rules are arguably unnecessary because HECM creditors must adhere to specific standards designed to protect both the creditor and the consumer, including robust appraisal rules.[38] In addition, a methodology for determining APORs for reverse mortgage transactions does not currently exist, so creditors would be unable to determine whether the APR of a given reverse mortgage transaction exceeded the rate thresholds defining a "higher-risk mortgage loan" (HPML in the final rule).

At the same time, the Agencies expressed concern that providing a permanent exemption for all reverse mortgage transactions, both private and HECM products, could deny key protections to consumers who rely on reverse mortgages. However, the Agencies proposed the exemption on at least a temporary basis, asserting that avoiding any potential disruption of this segment of the mortgage market in the near term would be in the public interest and promote the safety and soundness of creditors.

The Agencies requested comment on the appropriateness of this exemption. The Agencies also sought comment on whether available indices exist that track the APR for reverse mortgages and could be used by the Bureau to develop and publish an APOR for these transactions, or whether such an index could be developed, noting, for example, information published by HUD on HECMs, including the contract rate.[39]

As discussed further below, in § 1026.35(c)(2)(vi) of the final rule, the Agencies are adopting the proposed exemption for a "reverse-mortgage transaction subject to § 1026.33(a)."

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[37] *See* Bureau, *Reverse Mortgages: Report to Congress* 14, 70-99 (June 28, 2012), available at *http://www.consumerfinance.gov/reports/reverse-mortgages-report* (Bureau Reverse Mortgage Report).
[38] *See* HUD Handbook 4235.1, ch. 3.
[39] *See http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/rmra/oe/rpts/hecm/hecmmenu* (''Home Equity Conversion Mortgage Characteristics'').

Public Comments on the Proposal

National and State credit union trade associations, as well as a State banking trade association, supported the proposed exemption. However, appraiser trade association commenters generally believed that excluding appraisal protections would harm consumers, particularly senior citizens, and is contrary to public policy. Appraiser trade association, realtor trade association, and reverse mortgage lending trade association commenters suggested that any exemption should be limited to reverse mortgages under the FHA HECM program and not extended to proprietary products, because HECM consumers are afforded a comprehensive and mandatory set of appraisal protections. The reverse mortgage lending trade association also suggested circumstances under which reverse mortgages should be deemed qualified mortgages and, thus, qualify for an exemption on that basis. *See* section-by-section analysis of § 1026.35(c)(2)(i).

No commenters offered suggestions on an appropriate approach for developing an APOR for reverse mortgages. Appraiser trade associations, who only supported an exemption for HECMs, believed that the rules should apply to reverse mortgages even though indices do not currently exist. A reverse mortgage lending trade association believed that benchmark indices for reverse mortgages could be developed, but, supporting the proposed exemption, questioned whether one should be.

Discussion

The Agencies are adopting the proposed exemption for a "reverse-mortgage transaction subject to § 1026.33" for the same basic reasons discussed in the proposal, which were affirmed by most commenters. The Agencies share concerns expressed by some commenters about the risks to consumers of reverse mortgages generally, and of proprietary reverse mortgage loans in particular. Proprietary reverse mortgage loans are not insured by FHA or any other government entity, so payments are not guaranteed by the U.S. government to either consumers or creditors. By contrast, HECMs are insured by FHA and subject to a number of rules and restrictions designed to reduce risk to both consumers and creditors, including appraisal rules. *See* TILA section 129H(b)(4)(B), 15 U.S.C. 1639h(b)(4)(B).

As noted in the proposal, however, there is little to no market for proprietary reverse mortgages, and prospects for the reemergence of this market in the near-term are remote.[40] HECMs comprise virtually the entire reverse mortgage market and are subject to FHA's extensive HECM rules, which include appraisal requirements.[41] In addition, the Agencies believe that unwarranted creditor liability and operational risk could arise if the rule were applied to loans that a creditor cannot definitively determine are in fact subject to the rule, as is the case here, where no rate benchmark exists for measuring whether a reverse mortgage loan is an HPML. Thus, without an exemption for reverse mortgages, creditors would be susceptible to risks that could negatively affect their safety and soundness.

In reevaluating the proposed exemption, the Agencies also focused more attention on the fact that TILA's "higher-risk mortgage" appraisal rules apply only to closed-end products. Many (and historically most) reverse mortgages are open-end products. The Agencies are concerned about creating anomalies in the market and compliance confusion among creditors by applying one set of rules to closed-end reverse mortgages and another to open-end reverse mortgages. The Agencies note that compliance confusion among creditors can create burden and operational risk that can have a negative impact on the safety and soundness of the creditors. The Agencies are concerned that this bifurcation of the rule's application could also hinder creditors from

[40] Bureau Reverse Mortgage Report at 137-38.
[41] *See* HUD Handbook 4235.1, ch. 3.

offering a range of reverse mortgage product choices that support the creditors' loan portfolios while also benefitting consumers. In short, questions remain for the Agencies about whether this rule is the appropriate vehicle for addressing appraisal issues in the reverse mortgage market.

The Agencies remain concerned about the potential for abuse related to appraisals even with HECMs, which are subject to appraisal rules. Indeed, evidence exists that problems of property value inflation and fraudulent flipping occur even in the HECM market.[42] The Agencies plan to continue monitoring the reverse mortgage market closely and address appraisal issues as needed, including through consultations with the Bureau regarding any initiatives to revisit previously-issued reverse mortgage proposals (76 FR 58539, 53638-58659 (Sept. 24, 2012)).

For all these reasons, the Agencies have concluded that an exemption for all reverse mortgages at this time from this rule is in the public interest and promotes the safety and soundness of creditors.[43]

35(c)(3) Appraisals Required for Higher-Priced Mortgage Loans

35(c)(3)(i) In General

Consistent with TILA section 129H(a) and (b)(1), the proposal provided that a creditor shall 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

[42] Bureau Reverse Mortgage Report at 154, 157.

[43] By statute, the term "higher-risk mortgage" excludes any "qualified mortgage" and any "reverse mortgage loan that is a qualified mortgage." 15 U.S.C. 1639h(f). The Bureau was authorized by the Dodd-Frank Act to define the term "qualified mortgage" and has done so in its 2013 ATR Final Rule. However, the 2013 ATR Final Rule does not define the types of reverse mortgage loans that should be considered "qualified mortgages" because, by statute, TILA's ability-to-repay rules do not apply to reverse mortgages. *See* TILA section 129C(a)(8), 15 U.S.C. 1639c(a)(8). Thus the Agencies are not able to implement the precise statutory exemption for "reverse mortgage loans that are qualified mortgages." Instead, the exemption for reverse mortgages is based on the Agencies' express authority to exempt from TILA's "higher-risk mortgage" appraisal rules "a class of loans," if the exemption "is in the public interest and promotes the safety and soundness of creditors." TILA section 129H(b)(4)(B), 15 U.S.C. 1639h(b)(4)(B).

physical visit of the interior of the property that will secure the transaction. 15 U.S.C. 1639h(a) and (b)(1). In new § 1026.35(c)(3)(i), the final rule adopts this proposal without change.

35(c)(3)(ii) Safe Harbor

In the proposed rule, the Agencies proposed a safe harbor that would establish affirmative steps creditors can follow to ensure that they satisfy statutory obligations under TILA section 129H(a) and (b)(1). 15 U.S.C. 1639h(a) and (b)(1). This was done to address compliance uncertainties, which are discussed in more detail below.

The Agencies are adopting the final rule substantially as proposed. Specifically, under new § 1026.35(c)(3)(ii), a creditor would be deemed to have obtained a written appraisal that meets the general appraisal requirements now adopted in § 1026.35(c)(3)(i) if the creditor:

- Orders the appraiser to 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 (§ 1026.35(c)(3)(ii)(A));
- 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 as of the date the appraisal is signed (§ 1026.35(c)(3)(ii)(B));
- Confirms that the elements set forth in appendix N to part 1026 are addressed in the written appraisal (§ 1026.35(c)(3)(ii)(C)); and
- Has no actual knowledge to the contrary of facts or certifications contained in the written appraisal (§ 1026.35(c)(3)(ii)(D)).

The Agencies are also adopting proposed comments to the safe harbor. In particular, comment 35(c)(3)(ii)-1 clarifies that a creditor that satisfies the safe harbor conditions in

§ 1026.35(c)(3)(ii)(A)-(D) will be deemed to have complied with the general appraisal requirements of § 1026.35(c)(3)(i). This comment further clarifies that a creditor that does not satisfy the safe harbor conditions in § 1026.35(c)(3)(ii)(A)-(D) does not necessarily violate the appraisal requirements of § 1026.35(c)(3)(i).

Consistent with the proposal, appendix N to part 1026 provides that, to qualify for the safe harbor, a creditor must 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 included 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.

As discussed in the proposal, other than the certification for compliance with FIRREA title XI, the items in appendix N were derived from the Uniform Residential Appraisal Report (URAR) form used as a matter of practice in the residential mortgage industry. The final rule incorporates without change a proposed comment clarifying that a creditor need not look beyond the face of the written appraisal and the appraiser's certification to confirm that the elements in appendix N are included in the written appraisal. *See* § 1026.35(c)(3)(ii)(C)-1. However, as also provided in the proposal, the final rule provides that the safe harbor does not apply if the creditor has actual knowledge to the contrary of facts or certifications contained in the written appraisal. *See* § 1026.35(c)(3)(ii)(D).

Public Comments on the Proposal

The Agencies collectively received 17 comments from 13 trade groups, three financial institutions, and one bank holding company that addressed the proposed safe harbor. Of these, 14 commenters unequivocally supported the safe harbor. Several commenters requested clarification of certain issues. Two commenters recommended that the Agencies clarify that a lender has not necessarily violated the appraisal requirements when an appraisal does not meet the safe harbor's requirements. Another commenter recommended the final rule provide that a creditor may outsource the safe harbor requirements to a third party and that the creditor would be permitted to rely upon the third party's certification. The commenter also requested confirmation that creditors could use automated processes for checking whether the safe harbor's criteria were met.

The same commenter stated that the safe harbor did not indicate whether the creditor could rely on the face of the written appraisal report and the appraiser's certification. One commenter stated that the safe harbor was not clear regarding the scope and type of information that was required for some of the criteria. One commenter requested that the Agencies eliminate the certification for compliance with FIRREA.

Two commenters questioned implementation of the safe harbor and the creditor's responsibility under the safe harbor standard. These commenters recommended that the Agencies should use the same appraisal review standards that exist in FIRREA and the Interagency Appraisal and Evaluation Guidelines. One of the commenters questioned whether a creditor was being tasked under the safe harbor with adequate responsibility for review of an appraisal. This commenter noted that the proposal appeared to lower the bar for creditors in connection with appraisal review responsibilities. The commenter strongly opposed allowing creditors to perform appraisal review functions without necessarily using licensed or certified appraisers and recommended requiring lenders to use certified or licensed appraisers to perform any substantive appraisal review functions.

Discussion

As noted, the safe harbor is being adopted to address compliance uncertainties for creditors raised by the general appraisal requirements. Specifically, TILA section 129H(b)(1) requires that appraisals mandated by section 129H be performed by "a certified or licensed appraiser" who conducts a physical property visit of the interior of the mortgaged property. 15 U.S.C. 1639h(b)(1). The statute goes on to define a "certified or licensed" appraiser in some detail. TILA section 129H(b)(3), 15 U.S.C. 1639h(b)(3). The statute, however, is silent on how creditors should determine whether the written appraisals they have obtained comply with these statutory requirements.

TILA section 129H(b)(3) defines a "certified or licensed appraiser" as a person who is (1) certified or licensed by the State in which the property to be appraised is located, and (2) performs each appraisal in conformity with USPAP and the requirements applicable to appraisers in FIRREA title XI, and the regulations prescribed under such title, as in effect on the date of the appraisal. 15 U.S.C. 1639h(b)(3). These two elements of the definition of "certified or licensed appraiser" are discussed in more detail below.

Certified or licensed in the State in which the property is located. State certification and licensing of real estate appraisers has become a nationwide practice largely as a result of FIRREA title XI. Pursuant to FIRREA title XI, entities engaging in certain "federally related transactions" involving real estate are required to obtain written appraisals performed by an appraiser who is certified or licensed by the appropriate State. 12 U.S.C. 3339, 3341. As noted, to facilitate identification of appraisers meeting this requirement, the Appraisal Subcommittee of the FFIEC maintains an on-line National Registry of appraisers identifying all federally recognized State certifications or licenses held by U.S. appraisers.[44] 12 U.S.C. 3332, 3338.

Performs appraisals in conformity with USPAP and FIRREA. Again, TILA section 129H(b)(3) also defines "certified or licensed appraiser" as a person who performs each appraisal in accordance with USPAP and FIRREA title XI, and the regulations prescribed under such title, in effect on the date of the appraisal. 15 U.S.C. 1639h(b)(3). USPAP is a set of standards promulgated and interpreted by the Appraisal Standards Board of the Appraisal Foundation, providing generally accepted and recognized standards of appraisal practice for appraisers preparing various types of property valuations.[45] USPAP provides guiding standards, not specific methodologies, and application of USPAP in each appraisal engagement involves the application of professional expertise and judgment.

[44] The Agencies proposed to interpret the State certification or licensing requirement under TILA section 129H(b)(3) to mean certification or licensing by a State agency that is recognized for purposes of credentialing appraisers to perform appraisals required for federally related transactions pursuant to FIRREA title XI.
[45] *See* Appraisal Standards Bd., Appraisal Fdn., USPAP (2012-2013 ed.) *available at* http://www.uspap.org.

FIRREA title XI and the regulations prescribed thereunder regulate entities engaging in real estate-related financial transactions that are engaged in, contracted for, or regulated by the Federal financial institutions regulatory agencies.[46] *See* 12 U.S.C. 3339, 3350.

The statute does not specifically address Congress's intent in referencing USPAP and FIRREA title XI. Congress could have amended FIRREA title XI directly to expand the scope of the statute to subject all creditors to its requirements. Instead, Congress inserted language into TILA requiring that the *appraisers* who perform appraisals in connection with higher-risk mortgage loans comply with USPAP and FIRREA title XI. The statute is silent, however, as to the extent of *creditors*' obligations under the statute to evaluate appraisers' compliance.

The Agencies remain concerned that, practically speaking, a creditor might not be able to determine with certainty whether an appraiser complied with USPAP for a residential appraisal. An appraisal performed in accordance with USPAP represents an expert opinion of value. Not only does USPAP require extensive application of professional judgment, it also establishes standards for the scope of inquiry and analysis to be performed that cannot be verified absent substantially re-performing the appraisal. Conclusive verification of FIRREA title XI compliance (which itself incorporates USPAP) poses similar problems. On an even more basic level, it may not be possible for a creditor to determine conclusively whether the appraiser actually performed the interior visit required by TILA section 129H(a). Moreover, TILA subjects creditors to significant liability and risk of litigation, including private actions and class actions for actual and statutory damages and attorneys' fees. TILA section 130, 15 U.S.C. 1640.

[46] As discussed above in the section-by-section analysis of the definition of "certified or licensed appraiser" (§ 1026.35(c)(1)(i)), under FIRREA title XI, the Federal financial institutions regulatory agencies have issued regulations requiring insured depository institutions and their affiliates, bank holding companies and their affiliates, and insured credit unions to obtain written appraisals prepared by a State certified or licensed appraiser in accordance with USPAP for federally related transactions, including loans secured by real estate, exceeding certain dollar thresholds. *See* OCC: 12 CFR Part 34, Subpart C; FRB: 12 CFR part 208, subpart E, and 12 CFR part 225, subpart G; FDIC: 12 CFR part 323; and NCUA: 12 CFR part 722.

If TILA section 129H is construed to require creditors to assume liability under TILA for the appraiser's compliance with these obligations, the Agencies also remain concerned that it would unduly increase the cost and restrict the availability of higher-risk mortgage loans. Absent clear language requiring such a construction, the Agencies did not believe that the statute should be construed to intend this result.

As discussed in the proposal, the Agencies continue to be of the opinion that the safe harbor will be particularly useful to consumers, industry, and courts with regard to the statutory requirement that the appraisal be obtained from a "certified or licensed appraiser" who conducts each appraisal in compliance with USPAP and FIRREA title XI. While determining whether an appraiser is licensed or certified by a particular State is straightforward, USPAP and FIRREA provide a broad set of professional standards and requirements. The appraisal process involves the application of subjective judgment to a variety of information points about individual properties; thus, application of these professional standards is often highly context-specific. (The Agencies noted in the proposed rule, however, that a certification of USPAP compliance, one of the required safe harbor elements, is already an element of the URAR form used as a matter of practice in the industry.)

Regarding the first element of the safe harbor, that the creditor "order" that the appraiser perform the appraisal in conformity with USPAP and FIRREA, the Agencies generally understand that creditors seeking the safe harbor would include this assignment requirement in the engagement letter with the appraiser. *See* § 1026.35(c)(3)(ii)(A). Regarding specific comments received on the proposal, the Agencies note that the proposed staff commentary, now adopted, specifically addresses some of the issues the commenters raised. In particular, comment 35(c)(3)(ii)-1, discussed above, states that a creditor who does not satisfy the safe harbor conditions in § 1026.35(c)(3)(ii) does not necessarily violate the general appraisal requirements of § 1026.35(c)(3)(i). In addition, the Agencies note that another proposed element of the commentary, adopted as comment 35(c)(3)(ii)(C)-1, states a creditor need not look beyond the face of the written appraisal and the appraiser's certification to confirm that the elements in appendix N to this subpart are included in the written appraisal.

Some commenters sought clarification on whether the creditor could rely on the face of the appraisal report, and what scope and type of information is required for the appendix N criteria. As the Agencies discussed in the proposal, compliance with the appendix N safe harbor review requires the creditor to check certain elements of the written appraisal and the appraiser's certification on its face for completeness and internal consistency. The final rule, consistent with the proposed rule, does not require the creditor to make an independent judgment about or perform an independent analysis of the conclusions and factual statements in the written appraisal. As discussed above, the Agencies believe that imposing such obligations on the creditor could effectively require it to re-appraise the property. The Agencies also are retaining the requirement for the safe harbor that the appraiser certify, in the appraisal report, the appraiser's compliance with both USPAP and applicable FIRREA title XI regulations, although one commenter requested eliminating the certification of compliance with FIRREA.[47] This certification reflects that TILA requires creditors to obtain appraisals for "higher-risk mortgages" that are performed by the appraiser in conformity with the requirements of USPAP and applicable FIRREA title XI regulations. *See* TILA section 129H(b)(3)(B), 15 U.S.C. 1639h(b)(3)(B).

[47] The Agencies are aware that the URAR, currently used widely in the industry, includes a *pro forma* appraiser certification for USPAP compliance, but not for compliance with FIRREA Title XI appraisal regulations. Nonetheless, the URAR form accommodates "free text" additions by the appraiser, through which appraisers can add an appropriate FIRREA Title XI certification.

In response to comments about using third parties for the review of appendix N elements, the Agencies realize that some creditors may want to outsource the appraisal review function to confirm that the elements in appendix N are addressed in the written appraisal. Nonetheless, the Agencies emphasize that while a creditor may outsource this function to a third party as the creditor's agent, the creditor remains responsible for its agent's compliance with these requirements, just as if the creditor had performed the function itself, and the creditor cannot simply rely on the agent's certification. The same principle applies regarding a public comment seeking clarification about the use of automated review processes for the safe harbor; use of automated processes can be appropriate, but the creditor remains responsible for their effectiveness.[48]

As stated in the proposed rule, the Agencies are of the opinion that the safe harbor requirements would provide reasonable protections to consumers and compliance guidance to creditors. For the reasons previously provided and in light of commenters' general support, the Agencies have adopted the safe harbor provision as proposed.

35(c)(4) Additional Appraisal for Certain Higher-Risk Mortgage Loans

35(c)(4)(i) In General

Under TILA section 129H(b)(2), a creditor must obtain a "second appraisal" from a "different" certified or licensed appraiser if the higher-risk mortgage loan will "finance the purchase or 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." 15 U.S.C. 1639h(b)(2)(A). In the proposal, the Agencies interpreted this

[48] The Agencies also note that the Interagency Appraisal and Evaluation Guidelines provide comprehensive guidance on creditors' use of third parties for appraisal functions for institutions subject to the appraisal regulations under FIRREA title XI. *See Interagency Appraisal and Evaluation Guidelines*, 75 FR 77450, 77463-77464 (Dec. 10, 2010).

requirement to obtain a "second appraisal" to mean that the creditor must obtain an appraisal in addition to the one required under the general "higher-risk mortgage" appraisal rules in TILA section 129H(a) and (b)(1). *See* 15 U.S.C. 1639h(a) and (b)(1), implemented at new § 1026.35(b)(1)(i), discussed above. Thus, a creditor would be required to obtain two appraisals before extending a higher-risk mortgage loan to finance a consumer's acquisition of the property.

The Agencies proposed to implement the basic statutory requirement without material change. Thus, in "higher-risk mortgage loan" transactions under the proposal, creditors would have to apply additional scrutiny to properties being resold for a higher price within a 180-day period.

Using the exemption authority under TILA section 129H(b)(4)(B), the final rule adopts the proposal, but with substantive changes. 15 U.S.C. 1639h(b)(4)(B). Specifically, under new § 1026.35(c)(4)(i), a creditor may not extend an HPML that is not otherwise exempt from the appraisal requirements (see section-by-section analysis of § 1026.35(c)(2), above, and § 1026.35(c)(4)(vi), below) without obtaining, prior to consummation, two written appraisals, if:

- The seller is reselling the property within 90 days of acquiring it and the resale price exceeds the seller's acquisition price by more than 10 percent; or
- The seller is reselling the property within 91 to 180 days of acquiring it and the resale price exceeds the seller's acquisition price by more than 20 percent.

The Agencies are adopting a proposed comment to clarify that an appraisal that was previously obtained in connection with the seller's acquisition or the financing of the seller's acquisition of the property does not satisfy the requirements to obtain two written appraisals under § 1026.35(c)(4)(i). As discussed in more detail below, the Agencies are also adopting several other proposed comments to this rule without substantive change. *See* comments 35(c)(4)(i)-2 through -6.

Public Comments on the Proposal

The Agencies received over 50 comments concerning the proposal to implement the "second" appraisal requirement under TILA section 129H(b)(2) from trade associations, banks, credit unions, mortgage lending corporations, non-profit organizations, government-sponsored enterprises (GSEs), and individuals. The commenters offered responses to some of the questions the Agencies posed in the proposal and made suggestions for exemptions from the additional appraisal requirement. Exemptions and related public comments are discussed in the section-by-section analysis of § 1026.35(c)(4)(vi), below.

In the proposal, the Agencies requested comment on thirteen separate questions concerning the general requirement to obtain an additional appraisal and appropriate exemptions from this requirement. Public comments on proposals related to more specific rules for the additional appraisal are discussed in the section-by-section analysis of § 1026.35(c)(ii)-(v), below. On the general requirements adopted in § 1026.35(c)(4)(i), the Agencies received substantive comments on the following two questions.

Use of the term "additional appraisal" rather than "second appraisal." The Agencies used the term "additional appraisal" rather than "second appraisal" throughout the proposed rule and commentary because the term "second" may imply that the additional appraisal must be later in time than the first appraisal. In the proposal, the Agencies asked whether commenters agreed with the proposal's use of the term "additional appraisal" instead of the statutory term "second appraisal." The Agencies received six comments on this question. The commenters agreed that the use of the term "additional" appraisal is appropriate.

Three commenters requested clarification on how to distinguish between appraisals of different valuations in a lending decision, noting that the proposal did not specify which of the two required appraisals a creditor must rely on in extending a higher-risk mortgage loan if the appraisals provide different opinions of value.

Reliance on appraisal for seller's purchase of the property. The Agencies also requested comment on a proposed comment clarifying that an appraisal previously obtained in connection with the seller's acquisition or the financing of the seller's acquisition of the property cannot be used as one of the two required appraisals under the requirement for two appraisals under TILA section 129H(b)(2). 15 U.S.C. 1639h(b)(2). The Agencies received one comment on this question, which supported the Agencies' approach to this issue.

Discussion

Consistent with the statute and the proposal, new § 1026.35(c)(4)(i) requires a creditor to apply additional scrutiny to the value of properties securing HPMLs when they are being resold for a higher price within a 180-day period. The Agencies believe that the intent of TILA section 129H(b)(2), as implemented in § 1026.35(c)(4)(i), is to discourage fraudulent property "flipping," a practice in which a seller resells a property at an artificially inflated price within a short time period after purchasing it, typically after some minor renovations and frequently relying on an inflated appraisal to support the increase in value.[49] 15 U.S.C. 1639h(b)(2). Consumers who purchase properties at inflated values can be financially disadvantaged if, for example, they incur mortgage debt that exceeds the value of their dwelling at the time of the acquisition. The Agencies recognize that a property may be resold at a higher price within a

[49] *See* U.S. House of Reps., Comm. on Fin. Servs., *Report on H.R. 1728, Mortgage Reform and Anti-Predatory Lending Act*, No. 111-94, 59 (May 4, 2009) (House Report); Federal Bureau of Investigation, *2010 Mortgage Fraud Report Year in Review* 18 (August 2011), *available at* http://www.fbi.gov/stats-services/publications/mortgage-fraud-2010/mortgage-fraud-report-2010.

short timeframe for legitimate reasons, such as when a seller makes valuable improvements to the property or market prices increase. Section 1026.35(c)(4)(i) requires an additional appraisal analyzing the property's resale price to ensure that the increased sales price is appropriate.

In the proposal, the Agencies noted that this approach is generally consistent with rules promulgated by HUD to address property flipping in single-family mortgage insurance programs of the FHA. *See* 24 CFR 203.37a; 68 FR 23370, May 1, 2003; 71 FR 33138, June 7, 2006; 77 FR 71099, Nov. 29, 2012 (FHA Anti-Flipping Rules, or FHA Rules). In general, under the FHA Anti-Flipping Rules, properties that have been resold within 90 days are ineligible as security for FHA-insured mortgage financing. *See* 24 CFR § 237a(b)(2). Properties that have been resold 91 to 180 days from the seller's acquisition date are generally ineligible as security for FHA-insured mortgage financing if the sales price exceeds the seller's price by 100 percent. To obtain FHA insurance in this case, HUD requires additional documentation that must include an additional appraisal. *See* 24 CFR 237a(b)(3).

However, under temporary rules in effect until December 31, 2013, that waive the existing HUD anti-flipping regulations during the first 90-day period described above, FHA insurance may be obtained for a mortgage secured by a property resold within 90 days if certain conditions are met.[50] Among these conditions is a requirement for additional documentation if the sales price exceeds the seller's acquisition cost by more than 20 percent, including "a second appraisal and/or supporting documentation" verifying that the seller completed legitimate renovation, repair and rehabilitation work on the property to justify the price increase.[51]

[50] 77 FR 71099, 71100 (Nov. 29, 2012). The waiver rules were first issued in May 2010 and waived the existing regulations through December 31, 2011. 75 FR 38633 (May 21, 2010). The waiver was subsequently extended through December 31, 2012. 76 FR 81363 (Dec. 28, 2011).

[51] 77 FR 71099, 71100-71101 (Nov. 29, 2012).

Use of the term "additional appraisal" rather than "second appraisal." The Agencies are adopting use of the term "additional appraisal" rather than "second appraisal" throughout the final rule and commentary, as proposed. The Agencies are concerned that the term "second" may imply that the additional appraisal must be later in time than the first appraisal, when in some cases creditors might wish to order both appraisals simultaneously. In addition, creditors might not be able to identify easily which of the two appraisals is the "second appraisal" for purposes of complying with the prohibition on charging the consumer for any "second appraisal" under TILA section 129H(b)(2)(B). 15 U.S.C. 1639h(b)(2)(B) (implemented at § 1026.35(c)(4)(v), discussed in the section-by-section analysis of that provision, below). Public commenters supported use of the term "additional appraisal," and the Agencies do not believe that this term changes the substantive requirements of the statute.

Regarding concerns expressed by commenters about which appraisal to use for the credit decision when the two appraisals show different values, the Agencies acknowledge that the introduction of a second appraisal will sometimes place creditors in the position of exercising judgment as to which appraisal reflects the more robust analysis and opinion of property value. The Agencies recognize that creditors ordering two appraisals from different certified or licensed appraisers may likely receive appraisals providing different opinions. The Agencies decline to provide additional guidance on this matter in the final rule, however, because other rules and regulatory guidance address the issue and are more appropriate vehicles for this purpose. TILA section 129H does not require that the creditor use any particular appraisal, and the Agencies believe that a creditor should retain the discretion to select the most reliable valuation, consistent with applicable safety and soundness obligations and prudential regulatory guidance. 15 U.S.C. 1639h.

In particular, the Agencies noted in the proposal that TILA's valuation independence rules permit a creditor to obtain multiple valuations for the consumer's principal dwelling *to select the most reliable valuation*.[52] 12 CFR § 1026.42(c)(3)(iv). The Interagency Appraisal and Evaluation Guidelines also acknowledge that an institution may find it necessary to obtain another appraisal or evaluation of a property. In that case, the Guidelines affirm that the creditor is "expected to adhere to a policy of selecting the most credible appraisal or evaluation, rather than the appraisal or valuation that states the highest [or lowest] value."[53]

Reliance on appraisal for seller's purchase of the property. In comment 35(c)(4)(i)-1, the Agencies are adopting without change a proposed comment clarifying that an appraisal previously obtained in connection with the seller's acquisition or the financing of the seller's acquisition of the property cannot be used as one of the two required appraisals under the "additional" appraisal requirement. The Agencies believe that this clarification is consistent with the statutory purpose of TILA section 129H of mitigating fraud on the part of parties to the transaction. 15 U.S.C. 1639h. As noted, the one commenter who weighed in on this issue supported the Agencies' approach.

Section 1026.35(c)(4)(i) is consistent with the proposal in requiring the creditor to obtain the additional appraisal before consummating the HPML. TILA section 129H(b)(2) does not specifically require that the additional appraisal be obtained prior to consummation of the "higher-risk mortgage," but the Agencies believe that this timing requirement is necessary to effectuate the statute's policy of requiring creditors to apply greater scrutiny to potentially flipped properties that will secure the transaction. 15 U.S.C. 1639h(b)(2).

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[52] 75 FR 66554, 66561 (Oct. 28, 2010) (emphasis added).
[53] 75 FR 77450, 77458 (Dec. 10, 2010). The Guidelines refer creditors to the section of the Guidelines on "Reviewing Appraisals and Evaluations" for information on determining and documenting the credibility of an appraisal or evaluation. *See id.* at 77458, 77461-77463.

Section 1026.35(c)(4)(i) is consistent with the proposal in several other respects as well. First, the statute requires an additional appraisal "if the *purpose* of a higher-risk mortgage loan is *to finance the purchase or acquisition of the mortgaged property*," among other conditions. TILA section 129H(b)(2)(A), 15 U.S.C. 1639h(b)(2)(A) (emphasis added). Accordingly, § 1026.35(c)(4)(i) requires an additional appraisal only when the purpose of the HPML is to finance the acquisition of the consumer's principal dwelling – the requirement does not apply to refinance loans.

In addition, the final rule replaces the statutory term "mortgaged property" with the term "principal dwelling." TILA section 129H(b)(2)(A), 15 U.S.C. 1639h(b)(2)(A). The Agencies have made this change to be consistent with Regulation Z, which elsewhere uses the term "principal dwelling," most notably in the existing definition of HPML. *See* existing § 1026.35(a)(1) and the section-by-section analysis of revised § 1026.35(a)(1). Although a property that the consumer has not yet acquired will not at that time be the consumer's actual dwelling, existing commentary to Regulation Z explains that the term "principal dwelling" refers to properties that will become the consumer's principal dwelling within a year. *See* § 1026.2(a)(24) and comment 2(a)(24)-3. *See also* 12 CFR 34.202, comment 1 (OCC) and 12 CFR 226.43(a)(3), comment 1 (Board) (cross-referencing Regulation Z, which contains the Bureau's definition of "principal dwelling," and accompanying Official Staff Interpretations of Regulation Z for purposes of this rule). When referring to the date on which the seller acquired the "property" in § 1026.35(c)(4)(i)(A) and (B), however, the Agencies use the more general term "property" rather than "principal dwelling," because the subject property may not have been used as a principal dwelling when the seller acquired and owned it. The Agencies intend the term "principal dwelling" and "property" to refer to the same property.

Criteria for Whether an Additional Appraisal is Required—Acquisition Dates

As noted, the final rule requires a creditor to obtain two appraisals in two sets of circumstances: first, the seller is reselling the property within 90 days of acquiring it and the resale price exceeds the seller's acquisition price by more than 10 percent (new § 1026.35(c)(4)(i)(A)); and second, the seller is reselling the property within 91 to 180 days of acquiring it and the resale price exceeds the seller's acquisition price by more than 20 percent (new § 1026.35(c)(4)(i)(B)). To determine whether either set of circumstances exists and which price threshold applies, a creditor must determine the date on which the seller acquired the property and the date on which the consumer became obligated to acquire the property from the seller. These aspects of the final rule are discussed below.

Public Comments on the Proposal

The Agencies asked for public comment on several questions regarding the first of these conditions, § 1026.35(c)(4)(i)(A).

Treatment of non-purchase acquisitions and use of the term "acquisition." The proposal generally used the term "acquisition" instead of the longer statutory phrase "purchase or acquisition" to refer to the events in which the seller purchased or acquired the dwelling at issue. The Agencies proposed to use the sole term "acquisition" because this term, as clarified in a proposed comment adopted as comment 35(c)(4)-1, includes acquisition of legal title to the property, including by purchase. In the proposal, the Agencies interpreted "acquisition" broadly in order to encompass the broad statutory phrase "purchase or acquisition." Thus, as proposed, the additional appraisal rule would apply to a consumer's purchase of a property previously acquired by the seller through a non-purchase acquisition, such as inheritance, divorce, or gift.

In the proposal, the Agencies asked for comment on whether an additional appraisal should be required for consumer acquisitions where the property had been conveyed to the seller in a non-purchase transaction and where, arguably in the consumer's purchase, that seller may not have the same motive to earn a quick, unreasonable profit on a short-term investment. The Agencies also requested comment on how a creditor should calculate the seller's "acquisition price" in non-purchase scenarios. The Agencies offered the example of a case where the seller acquired the property by inheritance. In such a case, the seller's acquisition price could be considered "zero," which could make a subsequent sale offered at any price within 180 days subject to the additional appraisal requirement.

The Agencies also invited comment on whether the term "acquisition" might be over-inclusive in describing the consumer's transaction because non-purchase acquisitions by the consumer do not readily appear to trigger the additional appraisal requirement. For example, if the consumer acquired the property by means other than a purchase, he or she likely would not seek a mortgage loan to "finance" the acquisition.

Two commenters, national trade associations for appraisers, stated that they had no objections to excluding non-purchase transactions by either the seller or consumer from the additional appraisal requirement. A third commenter, a bank, affirmatively supported an exemption for non-purchase acquisitions, suggesting that such transactions are less likely to involve fraudulent flipping schemes.

The Agencies also asked for comment on whether the term "acquisition" is the appropriate term to use in connection with both the seller and mortgage consumer. In addition, the Agencies asked whether the term "acquisition" should 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. As noted in the proposal, the Agencies do not expect that fraudulent property flipping schemes would likely occur in this context. The Agencies also noted that existing commentary in Regulation Z clarifies that a "residential mortgage transaction" does not include transactions involving the consumer's principal dwelling when the consumer had previously purchased and acquired some interest in the dwelling, even though the consumer had not acquired full legal title, such as when one joint owner purchases the other owner's joint interest. *See* comments 2(a)(24)-5(i) and -5(ii); *see also* section-by-section analysis of § 1026.35(a)(1) (defining HPML and discussing the distinctions between the term "residential mortgage transaction" in Regulation Z and "residential mortgage loan" in the Dodd-Frank Act).

The Agencies received three comments as well on the appropriateness of using term "acquisition" rather than another term such as "purchase." Two commenters endorsed use of this term, without elaboration. A third commenter, a mortgage lending corporation, objected to the term "acquisition" and proposed the phrase "purchase acquisition" instead. The commenter suggested that consumers who acquire property through inheritance, divorce or other non-purchase means frequently want to sell the property quickly; therefore, application of the additional appraisal requirement is not appropriate and will needlessly delay such transactions.

The Agencies received three comments as well on the question of whether the additional appraisal should apply to partial interests in a transaction. One commenter, a regional trade association for credit unions, supported an exemption to cover a situation in which a consumer holds a partial interest in property and is acquiring the remainder of the interest from the seller. In support of its position, the commenter cited the commentary to Regulation Z mentioned in the proposal (comments 2(a)(24)-5(i) and -5(ii)), which clarifies that a "residential mortgage transaction" does not include transactions involving the consumer's principal dwelling when the consumer has a partial interest in the dwelling, such as when one joint owner purchases the other's joint interest. The other two commenters, national trade associations for appraisers, opposed exemptions for partial interest transactions, given what the commenters described as the inherent riskiness of higher-priced loans.

Discussion

Use of the term "acquisition." Consistent with the proposal, the Agencies have decided to adopt the proposal to use the term "acquisition" in place of the statutory phrase "purchase or acquisition" to refer to acquisitions by both the seller and the consumer. The Agencies are also adopting a proposed comment clarifying that, throughout § 1026.35(c)(4), the terms "acquisition" and "acquire" refer to the acquisition of legal title to the property pursuant to applicable State law, including by purchase. *See* comment 35(c)(4)-1. However, the Agencies are adopting a separate exemption from the additional appraisal requirement for HPMLs that finance the purchase of a property "[f]rom a person who acquired title to the property by inheritance or pursuant to a court order of dissolution of marriage, civil union, or domestic partnership, or of partition of joint or marital assets to which the seller was a party." This exemption and other exemptions from the additional appraisal requirement are discussed in more detail in the section-by-section analysis of § 1026.35(c)(4)(vii), below.

"Acquisition" by the seller. The final rule generally applies to transactions in which the seller had acquired the property without purchasing it, other than through divorce or inheritance. For example, the Agencies are concerned that fraudulent flipping can easily be accomplished when one party purchases a property and quickly deeds the property to another party (for example, as a gift), who then sells the property to an HPML consumer at an inflated price. If the

final rule applied only to instances in which the seller had purchased the property, the consumer's transaction would not trigger the added protections of the requirement to obtain two appraisals. By retaining the broader terms "acquisition" and "acquire," rather than a narrower term such as "purchase," the final rule ensures that two appraisals will be required to confirm the property's true value. *See* section-by-section analysis of § 1026.35(c)(4)(vi)(B) (explaining that, when a price paid by the seller for the property cannot be determined, two appraisals are required before an HPML can be extended). The different treatment by the rule for transactions involving seller acquisitions through inheritance or divorce are explained more fully in the section-by-section analysis of § 1026.35(c)(4)(vii), below.

"Acquisition" by the consumer. The Agencies believe that the terms "acquisition" or "acquire" to describe the consumer's acquisition of the property as well is desirable for consistency throughout the rule. The Agencies do not anticipate that the rule would apply where the consumer acquires the property without purchasing it. As a practical matter, if the consumer acquired the property by means other than a purchase, the rule would not come into play because he or she likely would not seek a mortgage to "finance" the acquisition. Moreover, if the consumer paid a nominal or no amount to acquire the property, the additional appraisal requirement would not likely be triggered—in this case, the consumer's price would rarely if ever exceed the seller's acquisition price, which is a condition for triggering the requirement for two appraisals. *See* § 1026.35(c)(4)(i)(B). In terms of whether and how the rule applies, however, the outcome of these scenarios would not change based on use of the term "acquisition" as opposed to a more precise term such as "purchase."

Seller. As proposed, the final rule uses the term "seller" throughout § 1026.35(c)(4) to refer to the party conveying the property to the consumer. The Agencies use this term to conform to the reference to “sale price” in TILA section 129H(b)(2)(A). 15 U.S.C. 1639h(b)(2)(A). Also, as discussed above, the Agencies do not foresee instances in which the rule would apply if the consumer acquired the property other than by a purchase transaction.

Agreement. The final rule follows the proposal in referring to the consumer’s “agreement” to acquire the property throughout § 1026.35(c)(4). A “sale price,” as referenced in TILA section 129H(b)(2)(A), is typically contained in a legally binding agreement or contract between a buyer and a seller. 15 U.S.C. 1639h(b)(2)(A). The commenters did not raise any objections to the use of this term as proposed.

Acquisition timeframe. As described above, TILA section 129H(b)(2)(A) requires creditors to obtain an additional appraisal for “higher-risk mortgages” that will finance the consumer’s purchase or acquisition if the following two circumstances are present: (1) the consumer is financing the purchase or acquisition of the mortgaged property from a seller within 180 days of the seller’s purchase or acquisition of the property; and (2) the current sale price of the property is higher than the price the seller paid for the property. 15 U.S.C. 1639h(b)(2)(A).

For a creditor to determine whether the first condition is met, the creditor has to compare two dates: the date of the consumer’s acquisition and the date of the seller’s acquisition. However, the statute does not provide specific guidance regarding the dates that a creditor must use to perform this comparison. TILA section 129H(b)(2)(A), 15 U.S.C. 1639h(b)(2)(A). To implement this provision, the Agencies proposed to require that the creditor 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. A proposed comment provided an illustration in which the creditor determines the seller acquired the property on April 17, 2012, and the consumer's acquisition agreement is dated October 15, 2012; an additional appraisal would not be required because 181 days would have elapsed between the two dates.

The Agencies did not receive public comment on these aspects of the proposal and adopt them without change in § 1026.35(c)(4)(i)(A) and (B), and comment 35(c)(4)(i)(A)-2.

Date the seller acquired the property. Regarding the date of the seller's acquisition, TILA section 129H(b)(2)(A) refers to the date of that person's "purchase or acquisition" of the property being financed by the higher-risk mortgage loan. 15 U.S.C. 1639h(b)(2)(A). Accordingly, § 1026.35(c)(4)(i)(A) and (B) refer to the date on which the seller "acquired" the property. Comment 35(c)(4)(i)-3, adopted from a proposed comment without change, clarifies that this refers to the date on which the seller became the legal owner of the property under State law, which the Agencies understand to be, in most cases, the date on which the seller acquired title. The Agencies have interpreted TILA section 129H(b)(2)(A) in this manner because the Agencies understand that creditors, in most cases, will not extend credit to finance the acquisition of a property from a seller who cannot demonstrate clear title. 15 U.S.C. 1639h(b)(2)(A). Also, as discussed above, the Agencies have proposed to use the single term "acquisition" because this term is generally understood to comprise acquisition of legal title to the property, including by purchase.

To assist creditors in identifying the date on which the seller acquired title to the property, comment 35(c)(4)(i)-3 is intended to clarify that the creditor may rely on records that provide information as to the date on which the seller became vested as the legal owner of the property pursuant to applicable State law. As provided in § 1026.35(c)(4)(vi)(A) and explained in comments 35(c)(4)(vi)(A)-1 through -3, the creditor may determine this date through reasonable diligence, requiring reliance on a written source document. The reasonable diligence standard is discussed further below under the section-by-section analysis of § 1026.35(c)(4)(vi)(A).

Date of the consumer's agreement to acquire the property. Regarding the date of the consumer's acquisition, TILA refers to the date on which the "higher-risk mortgage" consumer purchases or acquires the mortgaged property, but does not provide detail on how to define the consumer's acquisition. TILA section 129H(b)(2)(A), 15 U.S.C. 1639h(b)(2)(A). The Agencies proposed to interpret this provision to refer to "the date of the consumer's agreement to acquire the property." A proposed comment explained that, in determining this date, the creditor should use a copy of the agreement provided by the consumer to the creditor, and use the date on which the consumer and the seller signed the agreement. If the consumer and seller signed on different dates, the creditor should use the date on which the last party signed the agreement.

This comment is incorporated into the final rule without change as comment 35(c)(4)(i)-4. As explained in the proposal, the Agencies believe that use of the date on which the consumer and the seller agreed on the purchase transaction best accomplishes the purposes of the statute. This approach is substantially similar to existing creditor practice under the FHA Anti-Flipping Rule, which uses the date of execution of the consumer's sales contract to determine whether the restrictions on FHA insurance applicable to property resales are triggered. *See* 24 CFR 203.37a(b)(1). The Agencies have not interpreted the date of the consumer's acquisition to refer to the actual date of title transfer to the consumer under State law, or the date of consummation of the HPML, because it would be difficult if not impossible for creditors to determine, at the time that they must order an appraisal or appraisals to comply with § 1026.35(c), when title transfer or consummation will occur. The actual date of title transfer typically depends on whether a creditor consummates financing for the consumer's purchase and the seller delivers the deed to the consumer in exchange for the proceeds from the mortgage loan. Various factors considered in the underwriting decision, including a review of appraisals, will affect whether the creditor extends the loan. In addition, the Agencies are concerned that even if a creditor could identify a date certain by which the loan would be consummated and title would be transferred to the consumer, the creditor could potentially set a date that exceeds the 180-day time period to circumvent the requirements of § 1026.35(c)(4)(i).

Comment 35(c)(4)(i)-4 also clarifies that the date on which the consumer and the seller agreed on the purchase transaction, as evidenced by the date the last party signed the agreement, may not necessarily be the date on which the consumer became contractually obligated under State law to acquire the property. It may be difficult for a creditor to determine the date on which the consumer became legally obligated under the acquisition agreement as a matter of State law. Using the date on which the consumer and the seller agreed on the purchase transaction, as evidenced by their signatures and the date on the agreement, avoids operational and other potential issues because the Agencies expect that this date would be apparent on its face from the signature dates on the acquisition agreement.

Criteria for Whether an Additional Appraisal is Required—Acquisition Prices

TILA section 129H(b)(2)(A) requires creditors to obtain an additional appraisal if the seller had acquired the property "at a price that was lower than the current sale price of the property" within the past 180 days. 15 U.S.C. 1639h(b)(2)(A). To determine whether this statutory condition has been met, a creditor would have to compare the current sale price with the price at which the seller had acquired the property. Accordingly, the Agencies proposed to implement this requirement by requiring the creditor to compare the price paid by the seller to acquire the property with the price that the consumer is obligated to pay to acquire the property, as specified in the consumer's agreement to acquire the property. Thus, if the price paid by the seller to acquire the property is lower than the price in the consumer's acquisition agreement by a certain amount or percentage to be determined by the Agencies in the final rule, and the seller had acquired the property 180 or fewer days prior to the date of the consumer's acquisition agreement, the creditor would be required to obtain an additional appraisal before extending a higher-risk mortgage loan to finance the consumer's acquisition of the property.[54]

As noted above, the Agencies are adopting the general approach proposed of setting a particular price increase threshold that triggers the additional appraisal requirement, and are specifying the price increase thresholds as follows: A creditor is required to obtain two appraisals in two sets of circumstances—first, when the seller is reselling the property within 90 days of acquiring it at a price that exceeds the seller's acquisition price by more than 10 percent (new § 1026.35(c)(4)(i)(A)); and second, when the seller is reselling the property within 91 to 180 days of acquiring it at a price that exceeds the seller's acquisition price by more than 20 percent (new § 1026.35(c)(4)(i)(B)). This aspect of the final rule and related comments are discussed in greater detail below.

Price at which the seller acquired the property. TILA section 129H(b)(2)(A) refers to a property that the seller previously purchased or acquired "at a price." 15 U.S.C. 1639h(b)(2)(A). The proposal also referred to the "price" at which the seller acquired the property; a proposed comment clarified that the seller's acquisition price refers to the amount paid by the seller to acquire the property. The proposed comment also explained that the price at which the seller acquired the property does not include the cost of financing the property. This comment was

[54] The Agencies proposed a trigger for the additional appraisal requirement, adopted and revised in new § 1026.35(c)(4)(i)(B), as follows: "The price at which the seller acquired the property was lower than the price that the consumer is obligated to pay to acquire the property, as specified in the consumer's agreement to acquire the property from the seller, by an amount equal to or greater than *XX*." 77 FR 54722, 54772 (Sept. 5, 2012).

intended to clarify that the creditor should consider only the price of the property, not the total cost of financing the property.

The Agencies are adopting these aspects of the proposal without substantive change in § 1026.35(c)(4)(i)(A) and (B), and comment 35(c)(4)(i)-5.

Public Comments on the Proposal

The Agencies asked for comment on whether additional clarification was needed regarding how a creditor should identify the price at which the seller acquired the property. In particular, the Agencies also requested comment on how a creditor would 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. The Agencies understand that, in bulk sales, a sales price might be assigned to individual properties for tax or accounting reasons, but asked for public input on whether guidance may be needed for determining the sales price of a property for purposes of determining whether an additional appraisal is required. The Agencies also asked for comment on any operational challenges that might arise for creditors in determining purchase prices for homes purchased as part of a bulk sale transaction, as well as for views on whether any challenges presented could impede neighborhood revitalization in any way, and, if so, whether the Agencies should consider an exemption from the additional appraisal requirement for these types of transactions altogether.

An appraiser trade association stated that an appraiser's expertise is important in valuing properties that are part of a bulk sale. No other commenters commented on this question. In view of the value that appraisers can add in valuing properties as part of a bulk sale, and in the absence of requests or suggestions for additional guidance, the Agencies are adopting the rule as proposed with no additional provisions or clarifications regarding the purchase price of properties purchased in bulk sales.

Price the consumer is obligated to pay to acquire the property. TILA section 129H(b)(2)(A) refers to the "current sale price of the property" being financed by a higher-risk mortgage loan. 15 U.S.C. 1639h(b)(2)(A). The proposal referred to "the price that the consumer is obligated to pay to acquire the property, as specified in the consumer's agreement to acquire the property from the seller." The final rule adopts this language in § 1026.35(c)(4)(i)(A) and (B). The final rule also adopts a proposed comment clarifying that the price the consumer is obligated to pay to acquire the property is the price indicated on the consumer's agreement with the seller to acquire the property that is signed and dated by both the consumer and the seller. *See* comment 35(c)(4)(i)-6. In keeping with the proposal, comment 35(c)(4)(i)-6 also explains that the price at which the consumer is obligated to pay to acquire the property from the seller does not include the cost of financing the property to clarify that a creditor should only consider the sale price of the property as reflected in the consumer's acquisition agreement.

In addition, the comment refers to comment 35(c)(4)(i)-4 (providing guidance on the "date of the consumer's agreement to acquire the property," as discussed above). The intention of this cross-reference is to indicate that the document on which the creditor may rely to determine the consumer's acquisition price will be the same document on which a creditor may rely to determine the date of the consumer's agreement to acquire the property. Also tracking the proposal, comment 35(c)(4)(i)-6 further explains that the creditor is not obligated to determine whether and to what extent the agreement is legally binding on both parties. The Agencies expect that the price the consumer is obligated to pay to acquire the property will be apparent from the consumer's acquisition agreement.

Public Comments on the Proposal

The Agencies requested comment on whether the price at which the consumer is obligated to pay to acquire the property, as reflected in the consumer's acquisition agreement, provides sufficient clarity to creditors on how to comply while providing consumers adequate protection. The Agencies did not receive comments on this issue, and is adopting the proposal's use of the phrase "the price the consumer is obligated to pay to acquire the property, as specified in the consumer's agreement to acquire the property from the seller."

35(c)(4)(i)(A) and (B)

TILA section 129H(b)(2)(A) provides that an additional appraisal is required when the price at which the seller had purchased or acquired the property was "lower" than the current sale price and the resale occurs within 180 days of the seller's acquisition. 15 U.S.C. 1639h(b)(2)(A). TILA does not define the term "lower." Thus, as written, the statute would require an additional appraisal for any price increase above the seller's acquisition price, if the resale occurred within 180 days of the seller's acquisition. As discussed in more detail below, the Agencies do not believe that the public interest or the safety and soundness of creditors would be served if the law is implemented to require an additional appraisal for any increase in price. Accordingly, the Agencies proposed an exemption to the additional appraisal requirement for some threshold increase in the price. As described above, the proposal contained a placeholder for the amount by which the resale price would have to have exceeded the price at which the seller had acquired the property.

In § 1026.35(c)(4)(i)(A) and (B), the Agencies are adopting a tiered approach to the proposed exemption for certain price increases. Specifically:

- Section 1026.35(c)(4)(i)(A) exempts from the additional appraisal requirement HPMLs that finance the consumer's purchase of a property within 90 days of the seller's acquisition of the property at a price that does not exceed 10 percent of the seller's acquisition purchase price.
- Section 1026.35(c)(4)(i)(B), exempts from the additional appraisal requirement HPMLs that finance the consumer's purchase of a property within 91 to 180 days of the seller's acquisition of the property at a price that does not exceed 20 percent of the seller's acquisition price.

Public Comments on the Proposal

The Agencies solicited comment on potential exemptions for mortgage transactions that have a sale price that exceeds the seller's purchase price by a relatively small amount or by a certain percentage. The Agencies requested comment on whether a fixed dollar amount, a fixed percentage, or some alternate approach should be used to determine an exempt price increase, and what specific price threshold would be appropriate.

The Agencies received a large number of comments on these questions. The commenters generally endorsed the proposed exemption, based either on a dollar amount, or a percentage of the seller's acquisition price. Four commenters (a bank holding company, two national trade associations for mortgage lending companies and consumer and small-business lenders, and a large mortgage lending company) suggested that a 10 percent price increase exception would be appropriate. One of these commenters argued that 10 percent is a customary standard in the industry because it represents typical realtor and other closing costs.

A national trade association for community banks suggested a minimum of 15 percent. Two commenters, a regional trade association for credit unions and a community bank, argued that the exception should be at least 25 percent. One large national bank suggested a threshold of 5 percent. Another commenter, a credit union, suggested that an exemption be for the greater of three percent or a $10,000 increase in the price. A GSE suggested that the Agencies exempt from the second appraisal requirement sales that are subject to an "anti-flipping" clause. When an investor purchases a property in short sales from the GSEs, for example, certain clauses in the sales contract prohibit the investor from reselling that property for the first 30 days after the short sale purchase. The investor is then prohibited from reselling the property without justification and permission from the GSE for the next 31 to 90 days for a price that exceeds the seller's price by more than 20 percent.[55] Identical resale restrictions apply to investors purchasing property through a short sale under the Home Affordable Foreclosure Alternatives (HAFA) program.[56] Some commenters suggested that the Agencies incorporate FHA's regime as the standard for the higher-risk mortgage rule.

Discussion

As noted, the Agencies are adopting a tiered approach to the proposed exemption from the additional appraisal requirement of TILA section § 1026.35(c)(4)(i) for HPMLs that finance the resale of properties that do not exceed certain price increases from the prior sale. Specifically, § 1026.35(c)(4)(i)(A) exempts from the additional appraisal requirement HPMLs that finance the consumer's purchase of a property within 90 days of the seller's acquisition of the property where the resale price does not exceed 10 percent of the seller's acquisition price. Section 1026.35(c)(4)(i)(B), exempts from the additional appraisal requirement HPMLs that finance the consumer's purchase of a property within 91 to 180 days of the seller's acquisition of

[55] *See* Fannie Mae Single Family Servicing Guide Announcement SVC 2012-19, page 13; and Freddie Mac Single Family Seller Servicer Guide, Chapter B65.40(i).
[56] *See* U.S. Dept. of Treasury, Supplemental Directive 12-07 (Nov. 1, 2012).

the property where the resale price does not exceed 20 percent of the seller's acquisition price. In developing this approach, the Agencies reviewed public comments as well as other government standards and rules designed to curb harmful flipping in residential mortgage transactions. These included short sale reselling restrictions imposed by Fannie Mae, Freddie Mac and the U.S. Treasury Department,[57] as well as HUD's Anti-Flipping Rules – both HUD's existing regulations (12 CFR § 237a) and HUD rules currently in effect that temporarily "waive" existing regulations and replace them with other standards.[58]

The Agencies believe that short sale reselling restrictions of the GSEs and Treasury are instructive. Like these rules, the final rule incorporates a bifurcated approach to addressing fraudulent flipping, based on the number of days between the seller's purchase and the consumer's purchase.[59] The Agencies are not adopting an exemption for HPMLs financing sales subject to an anti-flipping clause, however. The Agencies are concerned that such an exemption would not be sufficiently protective of the HPML consumers the statute was intended to protect. If such an exemption covered only loans subject to GSE and Treasury anti-flipping clauses, HPML consumers purchasing homes from investors who acquired them from GSEs or Treasury would not receive the protection of the additional appraisal requirement. Meanwhile, HPML consumers purchasing homes from investors who acquired them from other creditors or investors would receive the protection of the additional appraisal requirement. It is unclear why HPML consumers in the latter case should receive these protections and consumers in the former case

[57] *See* Fannie Mae Single Family Servicing Guide Announcement SVC 2012-19, page 13; and Freddie Mac Single Family Seller Servicer Guide, Chapter B65.40(i); U.S. Dept. of Treasury, Supplemental Directive 12-07 (Nov. 1, 2012).

[58] *See*, *e.g.*, 77 FR 71099 (Nov. 29, 2012).

[59] As noted earlier, the GSE and Treasury short sale rules ban resales outright for 30 days after the short sale and also ban them if the sales price increases by more than 20 percent for resales in the next 31 to 90 days. *See* Fannie Mae Single Family Servicing Guide Announcement SVC 2012-19, page 13; and Freddie Mac Single Family Seller Servicer Guide, Chapter B65.40(i); U.S. Dept. of Treasury, Supplemental Directive 12-07 (Nov. 1, 2012).

should not. In addition, the purpose of the additional appraisal requirement in the final rule is to ensure a second opinion on the value of a purchased home; the purpose of anti-flipping clauses generally is to restrict the transaction entirely. Thus, these clauses may be instructive, but should not necessarily determine who receives the protection of this rule.

If an exemption for HPMLs financing sales subject to an anti-flipping clause covered loans subject to anti-flipping clauses more generally, the Agencies would be concerned about more HPML consumers not receiving the protections of the statute. Moreover, if creditors were concerned that the additional appraisal requirement might impede disposal of their distressed properties, they could devise "anti-flipping" clauses that would impose only minimal restrictions on the resale of those properties, simply to take advantage of the exemption. The Agencies recognize the importance to creditors and investors of being able to sell distressed properties in a timely manner to decrease losses. The Agencies further understand that restrictions on the resale of distressed properties purchased from creditors and investors can affect how quickly creditors and investors can dispose of these properties, and that creditors and investors design resale restrictions accordingly. However, the appraisal requirement under this final rule is not a restriction on resale by the seller; it is a requirement for additional documentation regarding the value of homes purchased by a certain subset of consumers who finance the transaction with an HPML.

The Agencies view the FHA Anti-Flipping Rules as also instructive for the final rule. In the preamble to its original Anti-Flipping Final Rule and waiver notices after it, HUD states that "fraudulent property flipping involves the rapid re-sale, often within days, of a recently acquired property."[60] HUD also states in its original final rule that "resales executed within 90 days imply

[60] *See*, *e.g.*, 68 FR 23370 (May 1, 2003); 77 FR 71099 (Nov. 29, 2012).

pre-arranged transactions that often prove to be among the most egregious examples of predatory lending."[61] Thus, under existing HUD regulations, FHA insurance is not available for loans that finance the purchase of a property within 90 days of the previous sale. *See* 12 CFR 237a(b)(2). HUD's rule is based on the conclusion that 90 days is a reasonable waiting period to ensure that legitimate rehabilitation and repairs of a property have occurred.[62]

HUD has also stated that a 180-day ban on eligibility for FHA insurance would have provided a disincentive to legitimate contractors who improve houses—thus increasing the stock of affordable housing.[63] Therefore, for transactions involving resales in the 91-180 day period, HUD will insure resales at any price, but requires additional documentation, which must include a second appraisal, if the price increase exceeds the seller's acquisition price by 100 percent. *See* 24 CFR 203.37a(b)(3).

The Agencies believe that HUD's basic approach – the use of more restrictive conditions for 90 days, followed by somewhat lesser restrictions for the next 90 days – has merit as an approach to combatting the kind of flipping with which Congress seemed concerned.[64] The Agencies recognize that, since issuing the regulation in 24 CFR 203.37a(b)(3), HUD has issued rules that temporarily replace its existing regulations, with the goal of encouraging investors to rehabilitate homes and thus help "stabilize real estate prices as well as neighborhoods and communities where foreclosure activity has been high."[65] Under these temporary rules, FHA

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[61] 68 FR 23370, 23372 (May 1, 2003).
[62]*See id.*
[63]*See id.*
[64] *See* U.S. House of Reps., Comm. on Fin. Servs., *Report on H.R. 1728, Mortgage Reform and Anti-Predatory Lending Act*, No. 111-94, 59 (May 4, 2009) (House Report); Federal Bureau of Investigation, *2010 Mortgage Fraud Report Year in Review* 18 (August 2011), *available at* http://www.fbi.gov/stats-services/publications/mortgage-fraud-2010/mortgage-fraud-report-2010. *See also* 71 FR 33138, 33141-33142 (June 7, 2006); HUD, Mortgagee Letter 2006-14 (June 8, 2006) ("FHA's policy prohibiting property flipping eliminates the most egregious examples of predatory flips of properties within the FHA mortgage insurance programs.").
[65] 77 FR 71099 (Nov. 29, 2012).

insurance is now available for loans that finance property resales within 90 days of the previous sale, as long as certain conditions are met. One condition is that "a second appraisal and/or supporting documentation" is required if the sales price exceeds the seller's acquisition price by more than 20 percent.[66] However, the Agencies recognize that these rules are designed to address a temporary market condition; the Agencies believe that the HPML appraisal rules must be designed to address property flipping beyond a temporary market condition.

At the same time, the Agencies believe that the approach adopted with respect to the additional appraisal requirement resembles the FHA waiver rules in some important ways that mitigate concerns about chilling investment. Like the FHA waiver rules, the final rule does not prohibit HPML financing of resales within 90 days (by contrast, the existing FHA regulations ban FHA insurance on resales within 90 days). Rather, the final rule imposes an additional condition on the transaction – namely, that the creditor must obtain a second appraisal for the creditor's use in considering the loan application and, more specifically, the collateral value of the dwelling that will secure the mortgage. The Agencies believe that this protection is consistent with congressional intent to provide additional protections for borrowers of loans considered by Congress to pose higher risks to those borrowers. Consistent with the views expressed by some commenters, however, the Agencies have determined that consumer protection is not served by requiring a second appraisal in circumstances where the increase generally is not indicative of a seller attempting to profit on a flip. The Agencies believe it is reasonable to expect a seller, faced with circumstances dictating resale of a dwelling that the

[66] *See id*. at 71100. A property inspection is also required. *See id.* at 71100-71101. For loans financing resales within 90 days where the sales price does not exceed the seller's acquisition price by more than 20 percent, FHA insurance is conditioned on the transactions being "arms-length, with no identity of interest between the buyer and seller or other parties participating in the sales transaction." *Id.* at 71100. HUD provides several examples of ways that lenders can ensure that there is no inappropriate collusion or agreement between parties. *Id.*

seller very recently acquired, to seek to recoup the seller's transaction costs on the purchase and resale, in addition to the seller's acquisition price. These costs may include fees from the seller's acquisition, such as mortgage application fees, origination points, escrow and attorney's fees, transfer taxes and recording fees, title search charges and title insurance premiums, as well as fees incurred in the resale, such as real estate commissions, seller-paid points, and other sales concessions on the resale. These costs will vary to some extent by State and by transaction. However, the Agencies believe that providing an allowance of 10 percent over the seller's acquisition price reasonably accommodates these transaction costs and strikes an appropriate balance with respect to ease of administration for purposes of the rule.

Regarding HPMLs that occur within 91 to 180 days, the final rule provides that an additional appraisal is required only if the property price increased by more than 20 percent of the seller's acquisition price. *See* § 1026.35(c)(4)(i)(B). In this way, the final rule provides a modest additional 10 percent allowance for legitimate repairs, and builds in a 90-day period in the interest of ensuring enough time to allow such repairs to be made. At the same time, the approach preserves added consumer protections in the first 90 days, when predatory flipping is most likely to occur. The Agencies recognize that this element of the final rule differs from the FHA Anti-Flipping Rules, which require additional documentation for a resale from 91 to 180 days only if the price increases by 100 percent of the seller's acquisition price. However, FHA insurance applies to HPMLs and non-HPMLs alike, and the Agencies believe that Congress intended special protections to apply to HPML consumers.

The Agencies believe that requiring an additional appraisal for HPMLs financing the purchase of a home being resold within a 180-day period, regardless of the amount of the price increase, could restrict home sales to HPML consumers, because investors might be less likely to sell properties to them. The additional appraisal rules could potentially affect the safety and soundness of creditors holding properties as a result of foreclosure or deed-in-lieu of foreclosure. This might arise if potential application of the two-appraisal requirement makes the properties less desirable for investors to purchase from financial institutions and rehabilitate for resale, out of investor concerns about the potential scope of the HPML requirement as applied to the pool of likely purchasers for their investment properties. This could create additional losses for creditors holding these properties. The Agencies do not believe that these potential negative impacts would be outweighed by consumer protections afforded by the additional appraisal requirement. The Agencies believe that the approach adopted by the final rule strikes the appropriate balance between allowing legitimate resales without undue restrictions and providing HPML consumers with additional protections from fraudulent flipping. For these reasons, the Agencies have concluded that the exemptions from the additional appraisal requirement reflected in § 1026.35(c)(4)(i)(A) and (B) are in the public interest and promote the safety and soundness of creditors.

35(c)(4)(ii) Different Certified or Licensed Appraisers

Under the proposed rule, the two appraisals required under the proposed paragraph now adopted as § 1026.35(c)(4)(i) could not be performed by the same certified or licensed appraiser. This proposal was consistent with TILA section 129H(b)(2)(A), which expressly requires that the additional appraisal must be performed by a "different" certified or licensed appraiser than the appraiser who performed the other appraisal for the "higher-risk mortgage" transaction. 15 U.S.C. 1639h(b)(2)(A).

As discussed in the proposal, during informal outreach conducted by the Agencies, some participants suggested that the Agencies impose additional requirements regarding the appraiser performing the second appraisal for the higher-risk mortgage loan, such as a requirement that the second appraiser not have knowledge of the first appraisal. Outreach participants indicated that this requirement would minimize undue pressure to value the property at a price similar to the value assigned by the first appraiser.

The Agencies explained that they did not propose any additional conditions on what it means to obtain an appraisal from a "different" certified or licensed appraiser because the Agencies expect that existing valuation independence requirements would be sufficient to ensure that the second appraiser performs an independent valuation. Rules to ensure that appraisers exercise their independent judgment in conducting appraisals exist under TILA (§ 1026.42), as well as FIRREA title XI.[67] In addition, the USPAP Ethics Rule requires that appraisers "perform assignments with impartiality, objectivity, and independence, and without accommodation of personal interests," and includes several examples of forbidden conduct related to this rule.[68] However, the Agencies requested comment on whether the rule should include additional conditions on what it means for the additional appraisal to be performed by a "different" appraiser. Specifically, the Agencies sought comment on whether the final rule should prohibit creditors from obtaining two appraisals by appraisers employed by the same appraisal firm, or who received the assignments from same appraisal management company (AMC).

The final rule follows the proposal and the statute in requiring that the additional appraisal must be performed by a "different" certified or licensed appraiser than the appraiser who performed the other appraisal for the HPML transaction. *See* § 1026.35(c)(4)(ii). In the

[67] *See* OCC: 12 CFR 34.45; Board: 12 CFR 225.65; FDIC: 12 CFR 323.5; NCUA: 12 CFR 722.5.
[68] Appraisal Standards Board, Appraisal Foundation, *Uniform Standards of Professional Appraisal Practice*, 2012-2013 Ed., pp. U-7 through U-9.

final rule, the Agencies also adopt a new comment clarifying what it means to obtain an appraisal from a "different" certified or licensed appraiser, discussed below.

Public Comments on the Proposal

The Agencies received approximately 36 comments relating to requirements that (1) the additional appraisal be performed by a "different" certified or licensed appraiser, discussed immediately below; (2) the additional appraisal include analysis of the sales price differences between the prior and current home sale transaction (*see* section-by-section analysis of § 1026.35(c)(4)(iv), below); and (3) the creditor may not charge the consumer for the additional appraisal (*see* section-by-section analysis of § 1035(c)(4)(v), below). These comments were submitted by banks and bank holding companies, credit unions, bank and credit union trade associations, and appraisal, realtor, and mortgage industry trade associations.

Of the commenters addressing the requests for comment on whether additional conditions should apply regarding the requirement that a "different" appraiser perform the additional appraisal, most urged that the rule allow a creditor to obtain two appraisals from the same appraisal firm or AMC, provided that they are performed by separate appraisers. Commenters favoring this approach suggested that allowing a creditor to use a single appraisal firm or AMC would reduce costs, ease compliance burdens, and mitigate concerns regarding the availability of appraisers, particularly in rural or sparsely populated areas. Several commenters noted that the use of a single appraisal firm or AMC would not weaken the different appraiser requirement since each appraisal is subject to USPAP and appraisal independence requirements. One commenter, however, stated the rule should prohibit a creditor from hiring appraisers from the same valuation firm and, with respect to AMCs, a creditor should be prohibited from hiring two appraisers through the same AMC if the AMC is an affiliate of the creditor.

Discussion

Consistent with the proposal, new § 1026.35(c)(4)(ii) provides that the two appraisals required under § 1026.35(c)(4)(i) may not be performed by the same certified or licensed appraiser. The Agencies are also adopting new comment 35(c)(4)(ii)-1, clarifying that the requirements that a creditor obtain two separate appraisals (§ 1026.35(c)(4)(i)), and that each appraisal be conducted by a "different" licensed or certified appraiser (§ 1026.35(c)(4)(ii)), indicate that the two appraisals must be conducted independently of each other. The comment explains that, if the two certified or licensed appraisers are affiliated, such as by being employed by the same appraisal firm, then whether they have conducted the appraisal independently of each other must be determined based on the facts and circumstances of the particular case known to the creditor.

As discussed in the proposal, the Agencies believe that the appraisal independence requirements of TILA (implemented at § 1026.42) help ensure that the two appraisals reflect valuation judgments that are independent of the creditor's loan origination interests and not biased by an appraiser's personal or business interest in the property or the transaction. TILA section 129E, 15 U.S.C. 1639e. In addition, FIRREA title XI includes rules to ensure that appraisers exercise their independent judgment in conducting appraisals, such as requirements that federally-regulated depositories separate appraisers from the lending, investment, and collection functions of the institution, and that the appraiser have "no direct or indirect interest, financial or otherwise, in the property."[69] As noted, USPAP's Ethics Rule, which applies to appraisers, also requires that appraisers "perform assignments with impartiality, objectivity, and independence, and without accommodation of personal interests," and includes several examples

[69] *See* OCC: 12 CFR 34.45; Board: 12 CFR 225.65; FDIC: 12 CFR 323.5; and NCUA: 12 CFR 722.5.

of prohibited conduct related to this rule.[70] As discussed in the section-by-section analysis of § 1026.35(c)(1)(a), compliance with USPAP is a condition of being a "certified or licensed appraiser" under TILA's "higher-risk mortgage" appraisal rules implemented in this final rule. TILA section 129H(b)(3), 15 U.S.C. 1639h(b)(3); § 1026.35(c)(1)(a).

Requirements for valuation independence for consumer credit transactions secured by the consumer's principal dwelling were adopted under amendments to TILA in the Dodd-Frank Act in 2010 and have been in effect since April of 2011. *See* 12 CFR 1026.42; 75 FR 66554 (Oct. 28, 2010), implementing TILA section 129E, 15 U.S.C. 1639e. The requirements in TILA, which carry civil liability, were designed to ensure that real estate appraisals used to support creditors' underwriting decisions are based on the appraiser's independent professional judgment, free of any influence or pressure that may be exerted by parties that have an interest in the transaction.

Existing appraisal independence requirements expressly prohibit appraisers, AMCs, or appraisal firms (all providers of settlement services) from having an interest in the property or transaction or from causing the value assigned to a consumer's principal dwelling to be based on any factor other than the independent judgment of the person preparing the appraisal. Material misstatements of the value are also prohibited for these parties, as is having a direct or indirect interest in the transaction, which prohibits these parties from being compensated based on the outcome of the transaction.

The Agencies understand that, in light of these rules, a principal reason that creditors contract with third-party AMCs and appraisal firms is to ensure that the appraisal function is independent from the loan origination function, as required by law. In addition, the creditor

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[70] Appraisal Standards Board, Appraisal Foundation, *Uniform Standards of Professional Appraisal Practice*, 2012-2013 Ed., pp. U-7 through U-9.

remains responsible for compliance with the appraisal requirements of § 1026.35(c), and both the creditor and the creditor's third party agent risk liability for violations of TILA's appraisal independence requirements.

At the same time, the Agencies have concerns about whether the unbiased appraiser independence will always be fully realized if, for example, the two appraisals are performed by appraisers employed by the same company. The Agencies recognize that in some cases, obtaining two appraisals from different appraisal firms might not be feasible, and moreover that appraisers working for the same company are cognizant of their independence, and indeed might not even interact at all. Thus, the rule is intended to allow flexibility in ordering the two appraisals from the same entity. However, as underscored in comment 35(c)(4)(ii)-1, in all cases the two appraisers should function independently of each other to ensure that in fact two separate and independent judgments of the property value are reflected in the required appraisals. If the creditor knows of facts or circumstances about the performance of the additional appraisal by the same firm indicating that the additional appraisal was not performed independently, the creditor should refrain from extending credit, unless the creditor obtains another appraisal.

35(c)(4)(iii) Relationship to General Appraisal Requirements

The proposed rule required that the additional appraisal meet the requirements of the first appraisal, including the requirements that the appraisal be performed by a certified or licensed appraiser who conducts a physical visit of the interior of the mortgaged property. *See* new § 1026.35(c)(3)(i). The Agencies expressed in the proposal the belief that this approach best effectuates the purposes of the statute. TILA section 129H(b)(1) provides that, "[s]ubject to the rules prescribed under paragraph (4), an appraisal of property to be secured by a higher-risk mortgage does not meet the requirements of this section unless it is performed by a certified or licensed appraiser who conducts a physical property visit of the interior of the mortgaged property." 15 U.S.C. 1639h(b)(1). The "second appraisal" required under TILA section 129H(b)(2)(A) is "an appraisal of property to be secured by a higher-risk mortgage" under TILA section 129H(b)(1). 15 U.S.C. 1639h(b)(1), (b)(2)(A). Therefore, to meet the requirements of TILA section 129H, the additional appraisal would be required to be "performed by a certified or licensed appraiser who conducts a physical visit of the interior of the property that will secure the transaction." TILA section 129H(b)(1), 15 U.S.C. 1639h(b)(1).

In addition, under TILA section 129H(b)(2)(A), the additional appraisal must analyze several elements, including "any improvements made to the property between the date of the previous sale and the current sale." 15 U.S.C. 1639h(b)(2)(A). The Agencies believe that the purposes of the statute would be best implemented by requiring the second appraiser to perform a physical interior property visit to analyze any improvements made to the property. Without an on-site visit, the second appraiser would have difficulty confirming that any improvements identified by the seller or the first appraiser were made.

In § 1026.35(c)(4)(iii), the Agencies are adopting the proposed requirement that, if the conditions requiring an additional appraisal are present (*see* new § 1026.35(c)(4)(i)), the creditor must obtain an additional appraisal that meets the requirements of the first appraisal, as provided in § 1026.35(c)(3)(i). In response to some commenters who expressed confusion about whether the creditor could rely on the safe harbor under § 1026.35(c)(3)(ii) in satisfying the general appraisal requirements under § 1026.35(c)(3)(i) for the additional appraisal, the Agencies are adopting a new comment. New comment 35(c)(4)(iii)-1 clarifies that when a creditor is required to obtain an additional appraisal under § 1026(c)(4)(i), the creditor must comply with the requirements of both § 1026.35(c)(3)(i) and § 1026.35(c)(4)(ii)-(v) for that appraisal. If the creditor meets the safe harbor criteria in § 1026.35(c)(3)(ii) for the additional appraisal, the creditor complies with the requirements of § 1026.35(c)(3)(i) for that appraisal.

35(c)(4)(iv) Required Analysis in the Additional Appraisal

The proposed rule required that the additional appraisal 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. The proposal specified that the changes in market conditions and improvements made to the property must be analyzed between the date of the seller's acquisition of the property and the date of the consumer's agreement to acquire the property. These proposed requirements are consistent with the statute, which requires that the additional appraisal "include an analysis of the difference in sale prices, changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale." TILA section 129H(b)(2)(A), 15 U.S.C. 1639h(b)(2)(A).

A proposed comment clarified that guidance on identifying the date the seller acquired the property could be found in the proposed comment now adopted as comment 35(c)(4)(i)(A)-3. This comment further stated that guidance on identifying the date of the consumer's agreement to acquire the property could be found in the proposed comment adopted as comment 35(c)(4)(i)(A)-2. The comment also stated that guidance on identifying the price at which the seller acquired the property could be found in the proposed comment adopted as comment 35(c)(4)(i)(B)-1 and that guidance on identifying the price the consumer is obligated to pay to acquire the property could be found in the proposed comment adopted as comment 35(c)(4)(i)(B)-2.

The Agencies requested comment on these proposed requirements for the additional appraisal, including the appropriateness of listing the requirement to analyze the difference in sales prices separately from the other two analytical requirements.

In § 1026.35(c)(4)(iii) and comment 35(c)(4)(iii)-1, the final rule adopts the proposed regulation text and comment with only one non-substantive change: for clarification about the subject of this subsection of the rule, the title of the subsection has been changed from "Requirements for the additional appraisal" to "Required analysis in the additional appraisal."

Public Comments on the Proposal

Two commenters addressed this issue. Of these, one commenter fully supported the proposed requirements for the additional appraisal, noting they are consistent with USPAP. The other commenter, however, suggested that the additional appraisal should not be required to include an analysis of the sale price paid by the seller and the acquisition price as set forth in the borrower's purchase agreement and improvements made to the property by the seller. The commenter argued that value should be based solely on the current market value of the property at the time of the appraisal and sale, of which the first appraisal should be determinative.

The Agencies also requested comment on the appropriateness of using, as prices that the additional appraisal must analyze, the terms "price at which seller acquired property" and "price consumer is obligated to pay to acquire property, as specified in consumer's agreement to acquire property from seller." Further, the Agencies asked for comment on the appropriateness of using, as the dates the additional appraisal must analyze in considering changes in market conditions and improvements to property, the terms "date seller acquired property" and "date of consumer's agreement to acquire property." No comments were received on this issue.

Discussion

After consideration of public comments, the Agencies believe that the proposal is appropriate to adopt without substantive change, as discussed above. Regarding the comment that the additional appraisal should not include an analysis of the property price increase between the seller's price and the consumer's price, but that market value as reflected in the first appraisal should be determinative, the Agencies point out that the analysis in the additional appraisal required under new § 1026.35(c)(4)(iii) is mandated by statute. Moreover, the Agencies believe that the intent of these requirements is to ensure that creditor, in considering the value of the collateral in connection with its lending decision, is presented with information focused specifically on factors that reasonably increase collateral value in a relatively short period, such as market changes and property improvements. These statutory requirements are designed to serve as a backstop for consumers against fraud in flipped transactions and thus are implemented largely unchanged in the final rule.

35(c)(4)(v) No Charge for the Additional Appraisal

Under the proposed rule, if a creditor must obtain a second appraisal, it may charge the consumer for only one of the appraisals. The Agencies proposed a comment clarifying that this rule means that the creditor would be prohibited from imposing a fee specifically for that appraisal or by marking up the interest rate or any other fees payable by the consumer in connection with the higher-risk mortgage loan. The proposal was designed to implement TILA section 129H(b)(2)(B), which provides that "[t]he cost of the second appraisal required under subparagraph (A) may not be charged to the applicant." 15 U.S.C. 1639h(b)(2)(B).

The Agencies requested comment on this proposed approach, and whether there might be particular ways that the creditor could identify the appraisal for which the consumer may not be charged in cases where, for example, the appraisals are ordered simultaneously.

The proposed rule and clarifying comment are adopted without change in § 1026.35(c)(4)(v) and comment 35(c)(4)(v)-1.

Public Comments on the Proposal

Most commenters were strongly opposed to requiring the additional appraisal to be obtained at the creditor's expense. While a number of commenters acknowledged that the requirement is statutorily mandated under Dodd-Frank they were nevertheless critical of it, cautioning that the requirement would ultimately limit the availability of credit to consumers. Many commenters indicated that the cost of an additional appraisal would make the loan too costly or unprofitable, leading creditors to cease offering higher-risk mortgage loans to riskier borrowers. Several commenters argued it is unfair for creditors to bear the cost responsibility of a second appraisal, where the applicant has no incentive to go forward with the loan and there is no guarantee that the loan will be consummated. Commenters urged the Agencies to exercise their exemption authority to permit creditors to charge consumers a reasonable fee for the additional appraisal. Alternatively, one comment letter recommended that creditors be prohibited from charging a direct cost for the additional appraisal but not an indirect cost.

Discussion

As noted, TILA section 129H(b)(2)(B) provides that "[t]he cost of the second appraisal required under subparagraph (A) may not be charged to the applicant." 15 U.S.C. 1639h(b)(2)(B). Consistent with the statute and the proposal, § 1026.35(c)(4)(v) provides that "[i]f the creditor must obtain two appraisals under paragraph (c)(4)(i) of this section, the creditor may charge the consumer for only one of the appraisals." As clarified in comment 35(c)(4)(v)-1, adopted without change from the proposal, the creditor would be prohibited from imposing a fee specifically for that appraisal or by marking up the interest rate or any other fees payable by the consumer in connection with the higher-risk mortgage loan (now HPML).

The proposed comment adopted in the final rule also explains that the creditor would be prohibited from charging the consumer for the "performance of one of the two appraisals required under § 1026.35(c)(4)(i)." This comment is intended to clarify that the prohibition on charging the consumer under § 1026.35(b)(4)(v) applies to the cost of providing the consumer with a copy of the appraisal, not to charges for the cost of performing the appraisal. As implemented by new § 1026.35(c)(6)(iv), TILA section 129H(c) prohibits the creditor from charging the consumer for one copy of each appraisal conducted pursuant to the higher-risk mortgage rule. 15 U.S.C. 1639h(c); *see also* section-by-section analysis of § 1026.35(c)(6)(iv), below. As in the proposal, the final rule does not use the statutory term "second" appraisal, but instead refers to the "additional" appraisal because, in practice, a creditor ordering two appraisals at the same time may not know which of the two appraisals would be the "second" appraisal. The Agencies understand that the additional appraisal could be separately identified because it must contain an analysis of elements in proposed § 1026.35(c)(4)(iv). The Agencies also understand that appraisers may perform such an analysis as a matter of routine, and that it may be difficult to distinguish the two appraisals on that basis.[71]

In addition, the final rule also tracks the proposal in prohibiting the creditor from charging "the consumer," rather than, as in the statute, the "applicant." The Agencies believe

[71] *See, e.g.,* USPAP Standards Rule 1-5(b) (requiring an appraiser to "analyze all sales of the subject property that occurred within the three years prior to the effective date of the appraisal"); USPAP Standards Rule 1-4(a) (stating that "an appraiser must analyze such comparable sales data as are available to indicate a value conclusion") and USPAP Standards Rule 1-4(f) (stating that "when analyzing anticipated public or private improvements . . . an... appraiser must analyze the effect on value, if any, of such anticipated improvements to the extent they are reflected in market actions."

that use of the broader term "consumer" is necessary to clarify that the creditor may not charge the consumer for the cost of the additional appraisal after consummation of the loan.

Regarding commenters' requests that creditors be permitted to charge the consumer for the additional appraisal, the Agencies point out that they do not jointly have authority to provide for adjustments and exceptions to TILA under TILA section 105(a), which belongs to the Bureau alone. 15 U.S.C. 1604(a). The prohibition on charging the consumer for the additional appraisal is mandated by statute. The Agencies have implemented this statutory prohibition with certain clarifications appropriate to carry out the statutory mandate consistently with their general authority to interpret the statute – specifically clarifying in commentary that the creditor is prohibited from imposing a fee specifically for that appraisal or by marking up the interest rate or any other fees payable by the consumer in connection with the higher-risk mortgage loan. *See* § 1026.35(c)(4)(v) and comment 35(c)(4)(v)-1.

The Agencies recognize that neither the statute's plain language nor the final rule precludes a creditor from spreading costs of additional appraisals over a large number of loans and products. The Agencies believe, however, that Congress clearly intended to ensure that the consumer offered an HPML, who may have limited credit options, not be exclusively affected by having to bear this cost in full. The Agencies further believe that the final rule is consistent with this statutory purpose.

35(c)(4)(vi) Creditor's Determination of Prior Sale Date and Price

35(c)(4)(vi)(A) Reasonable Diligence

The Agencies proposed to require that the creditor have exercised reasonable diligence to support any determination that an additional appraisal under § 1026.35(c)(4)(i) is *not* required. (For a discussion of the factors triggering the requirement, see the section-by-section analysis of

§ 1026.35(c)(4)(i)(A) and (B), above.) Absent an exemption (*see* § 1026.35(c)(2) and (c)(4)(vii)), an additional appraisal would always be required for an HPML where the creditor elected not to conduct reasonable diligence, could not find the relevant sales price and sales date information, or where the information found led to conflicting conclusions about whether an additional appraisal were required. *See* section-by-section analysis of § 1026.35(c)(4)(vi)(B), below.

To help creditors meet the proposed reasonable diligence standard, the Agencies proposed that creditors be able to rely on written source documents that are generally available in the normal course of business. Accordingly, a proposed comment clarified that a creditor has acted with reasonable diligence to determine when the seller acquired the property and whether the price at which the seller acquired the property is lower than the price reflected in the consumer's acquisition agreement if, for example, the creditor bases its determination on information contained in written source documents, as discussed below.

The proposed comment provided a list of written source documents, not intended to be exhaustive, that the creditor could use to perform reasonable diligence as follows: a copy of the recorded deed from the seller; a copy of a property tax bill; a copy of any owner's title insurance policy obtained by the seller; a copy of the RESPA settlement statement from the seller's acquisition (*i.e.*, the HUD-1 or any successor form[72]); a property sales history report or title report from a third-party reporting service; sales price data recorded in multiple listing services; tax assessment records or transfer tax records obtained from local governments; a written appraisal, including a signed appraiser's certification stating that the appraisal was performed in

[72] As explained in a footnote in the proposed comment, the Bureau's 2012 TILA-RESPA Proposal contains a proposed successor form to the RESPA settlement statement. *See* §1026.38 (Closing Disclosure Form) of the Bureau's 2012 TILA-RESPA Proposal, 77 Fed. Reg. 51116 (Aug. 23, 2012).

conformity with USPAP, that shows any prior transactions for the subject property; a copy of a title commitment report; or a property abstract.

The proposed comment contained a footnote explaining that a "title commitment report" is a document from a title insurance company describing the property interest and status of its title, parties with interests in the title and the nature of their claims, issues with the title that must be resolved prior to closing of the transaction between the parties to the transfer, amount and disposition of the premiums, and endorsements on the title policy. The footnote also explained that the document is issued by the title insurance company prior to the company's issuance of an actual title insurance policy to the property's transferee and/or creditor financing the transaction. In different jurisdictions, this instrument may be referred to by different terms, such as a title commitment, title binder, title opinion, or title report.

An additional proposed comment explained that reliance on oral statements of interested parties, such as the consumer, seller, or mortgage broker, do not constitute reasonable diligence. The Agencies explained in the proposal that they do not believe that creditors should be permitted to rely on oral statements offered by parties to the transaction because they may be engaged in the type of fraud the statutory provision was designed to prevent.

In new § 1026.35(c)(4)(vi) and appendix O, the Agencies are adopting the reasonable diligence standard and proposed comments discussed above without material change. Certain technical changes to the regulation text and corresponding comments have been made for clarity, without substantive change intended. The Agencies are also adding a new comment providing guidance on written source documents that show only an estimated or assumed value for the seller's acquisition price. Specifically, this new comment clarifies that, if a written source document describes the seller's acquisition price in a manner that indicates that the price described is an estimated or assumed amount and not the actual price, the creditor should look at an alternative document to satisfy the reasonable diligence standard in determining the price at which the seller acquired the property. *See* comment (c)(4)(vi)(A)-1.

The reasons for the final rule and revisions to the proposal are discussed in more detail below.

Public Comments on the Proposal

The Agencies requested comment on a number of aspects of the reasonable diligence standard and accompanying comments. Specifically, comment was requested on whether the list of written source documents now adopted in comment 35(c)(4)(vi)-1 would provide reliable information about a property's sales history and could be relied on in making the additional appraisal determination, provided they indicate the seller's acquisition date or the seller's acquisition price.

The Agencies also requested comment on whether a creditor should be permitted to rely on a signed USPAP-compliant written appraisal prepared for the transaction to determine the seller's acquisition date and price, and whether a creditor could take any specific measures to ensure that the appraiser is reporting prior sales accurately. The Agencies indicated particular interest in commenters' view on whether, for creditors that are required to select an independent appraiser, such as creditors subject to the Federal financial institutions regulatory agencies' FIRREA title XI rules, the creditor's selection of an independent appraiser is sufficient to address the concern that the appraiser may be colluding with a seller in perpetrating a fraudulent flipping scheme.

Noting that public documents listed might not include the requisite information and that there might be risks inherent in allowing reliance on seller-provided documents, the Agencies also asked whether non-public information sources are likely to be more easily available or more accurate than public ones.

Finally, the Agencies requested comment on the proposed clarification that reliance on oral statements alone would not be sufficient to satisfy the reasonable diligence standard, specifically on whether circumstances exist in which oral statements offered by parties to the transaction could be considered reliable if documented appropriately, and how such statements should be documented to ensure greater reliability.

General comments on the list of source documents. Four commenters responded to general questions about whether the list of source documents was appropriate. Several of these commenters affirmed the Agencies' understanding that some jurisdictions have a lengthy delay between the time a purchase and sale transaction is closed and the recording of the deed. In those cases, these commenters averred, that delay would preclude using the deed as a source document since it would not be available to the creditor for its due diligence.

One commenter suggested that the seller be required to provide the source documents rather than the creditor having to obtain them from the public records, although recognizing the possibility that the seller may intentionally alter the documents to his needs. Appraiser trade associations concurred with the proposal's "flexible approach" to due diligence sources in allowing use of seller-provided documents. This commenter believed that this approach would mitigate the possibility that a lack of access to or availability of source documents would result in a "chilling effect" on mortgage lending. Another commenter noted that the borrower's creditor would have difficulty obtaining copies of documents from the seller. This commenter recommended that the rule provide that, where none of the source documents provides the required information, the creditor may provide a certified or attested document signed by the parties as sufficient evidence of "reasonable diligence."

Use of the first appraisal in the transaction. All three comments relating to the question of whether the final rule should allow creditors to use and rely on the entire contents of USPAP-compliant appraisals prepared by certified and licensed appraisers supported allowing this. Nevertheless, commenters noted that oversight of appraisal services by users and regulators would be necessary, as would vigorous enforcement if appraisers violate the requirements. One commenter recommended that creditors use data from multiple listing services captured by the appraisal to obtain prior sales price information. That commenter also requested clarification in the rule that where multiple listing documents have different sales price data, that the creditor is deemed to have complied with the rule if it chooses to use any one.

Additional comments from appraiser trade associations agreed with allowing creditors to rely on appraisal information relating to sellers' acquisition dates but only so far as that information is available to the appraiser in the normal course of business, which is all that is required of an appraiser under USPAP. These commenters urged the Agencies to be careful not to impose requirements on appraisers relating to information, data, and analysis that are not required of appraisers in a typical USPAP-compliant report.

Use of seller-provided and other non-public documents. Several commenters recognized that sometimes creditors have no other reliable sources than seller-provided or other non-public documents. Appraiser association commenters proposed that the Agencies consider a "good-faith" exception that would allow creditors to rely on non-traditional sources of information when more reliable ones are not available. These commenters reasoned that this exception would balance the underlying public policy of supporting "higher-risk mortgage loans" (now

HPMLs) when no other loan product is available or feasible, against the risk that creditors will rely on bad information.

Reliability of oral statements. No commenters opposed the proposed comment, adopted as comment 35(c)(4)(vi)-2, clarifying that reliance on oral statements alone would not satisfy the reasonable diligence standard. Appraiser trade associations generally shared the Agencies' concern about the potential risk of relying on information presented by interested parties.

Discussion

As noted, the Agencies are adopting the proposed reasonable diligence standard and associated comments without material change. The Agencies believe that this standard is important to facilitate compliance because it may be difficult in some cases for a creditor to know with absolute certainty that the criteria triggering the additional appraisal requirement have been met. *See* § 1026.35(c)(4)(i)(A) and (B). Similarly, a creditor may have difficulty knowing whether it relied on the "best information" available in making the determination, which could require that creditors perform an exhaustive review of every document that might contain information about a property's sales history and unduly limit the availability of credit to higher-risk mortgage consumers.

Regarding the proposed list of source documents on which creditors may appropriately rely, now adopted in appendix O, the Agencies note that the first four listed items would be voluntarily provided directly or indirectly by the seller, rather than collected from publicly available sources. As did commenters, the Agencies recognize that permitting the use of these documents presents the risk that the creditor would be presented with altered copies. Balanced against this risk, however, is the concern that no information sources are publicly available in non-disclosure jurisdictions and jurisdictions with significant lag times before public land records are updated to reflect new transactions.[73] The Agencies are concerned that, unless the creditor can rely on other sources, such as sources provided by the seller, the higher-risk mortgage transaction may not proceed at all, or could proceed only with an additional appraisal containing a limited form of the analysis that would be required by TILA section 129H(b)(2)(A). 15 U.S.C. 1639h(b)(2)(A). The proposed footnote explaining the term "title commitment report" (Item 9), described above, is moved in the final rule to new comment 1 of appendix O.

As noted, new comment 35(c)(4)(vi)(A)-1 clarifies that, if a written source document describes the seller's acquisition price in a manner that indicates that the price described is an estimated or assumed amount and not the actual price, the creditor should look at an alternative document to satisfy the reasonable diligence standard in determining the price at which the seller acquired the property.

Regarding a commenter's recommendation that a creditor be permitted to provide a certified or attested document signed by the parties as sufficient evidence of "reasonable diligence," the Agencies believe that this allowance could easily be abused and would not constitute sufficient diligence. Instead, as discussed in the section-by-section analysis of § 1026.35(c)(4)(vi)(B) below, the Agencies believe that the consumer protection purposes of the statute are better served by simply requiring two appraisals where reliable written documentation of the sales price and date are unavailable. Similarly, regarding questions about multiple listing documents that have different sales price data, the Agencies believe that in cases of conflicting listing price information, the consumer protection purposes of the statute are best served if the

[73] During informal outreach conducted by the Agencies for the proposal, representatives of large, small, and regional lenders expressed concern that in some cases, a creditor may be unable to determine the seller's date and price due to information gaps in the public record. The Agencies also understand that a creditor may not be able to determine prior transaction data because of delays in the recording of public records. The Agencies also understand that certain "non-disclosure" jurisdictions do not make the price at which a seller acquired a property available in the public records. These concerned were affirmed by public comments on the proposal.

creditor obtains better information from other sources through the exercise of reasonable diligence and, failing that, obtains a second appraisal. *See* section-by-section analysis of § 1026.35(c)(4)(vi)(B), below.

On the recommendation that the Agencies consider a "good-faith" exception that would allow creditors to rely on non-traditional sources of information, the Agencies believe that the "reasonable diligence" standard alone is more appropriate and addresses the commenters' concerns. Under this standard, a broad array of widely used public and non-public documents, set forth in the non-exhaustive list under comment 35(c)(4)(vi)-1, could be relied on by creditors. In short, the Agencies expect that, with the parameters established in this comment, the rule will appropriately balance the need to assure access to HPML credit against the risk that creditors will rely on bad information.

Regarding reliance on another USPAP-compliant appraisal to satisfy the reasonable diligence standard, the Agencies are revising the proposed list to clarify that a creditor would not be permitted to rely on an appraisal other than the one prepared for the creditor for the subject HPML. Specifically, the Agencies are revising Item 8, which, in the proposal read as follows: "A written appraisal signed by an appraiser who certifies that the appraisal has been performed in conformity with USPAP that shows any prior transactions for the subject property." In the final rule, this comment has been revised to read as follows: "A written appraisal performed in compliance with § 1026.35(c)(3)(i) for the same transaction that shows any prior transactions for the subject property." The Agencies are concerned that, as proposed, this item in the written source document list could lead creditors to believe that appraisals performed for the seller's acquisition or other appraisals that might otherwise be considered "stale" could be relied on. As revised, the list item allows reliance specifically on an appraisal performed in compliance with the HPML appraisal requirements for the same HPML transaction. That means that the appraisal would have to have been performed by a state-certified or -licensed appraiser in conformity with USPAP and FIRREA.

On a related issue, the Agencies emphasize that allowing the creditor to rely on the first appraisal for prior sales information does not require more of appraisers than does USPAP. Again, the first appraisal must be performed in compliance with USPAP and FIRREA. The Agencies understand that USPAP Standards Rule 1-5 requires appraisers to "analyze all sales of the subject property that occurred within the three (3) years prior to the effective date of the appraisal" if that information is available to the appraiser "in the normal course of business."[74] If the appraiser did not include that information because it was not available to the appraiser under the USPAP standard, the creditor must turn to another document under the reasonable diligence standard.

Overall, due to the many requirements to which the first appraisal is subject, including independence requirements under TILA (implemented by § 1026.42), and in the absence of public comments to the contrary, the Agencies expect that, in cases where the appraiser has provided a price, a creditor generally could rely on the first appraisal prepared for the HPML transaction to satisfy the reasonable diligence standard under § 1026.35(c)(4)(vi)(A). The exception would be circumstances under which other information obtained by the creditor makes reliance on the price unreasonable. *See also* section-by-section analysis of § 1026.35(c)(4)(ii), above.

[74] Appraisal Standards Bd., Appraisal Fdn., Standards Rule 1-5, USPAP (2012-2013 ed.).

Comment 35(c)(4)(vi)(A)-2 clarifies that reliance on oral statements of interested parties, such as the consumer, seller, or mortgage broker, does not constitute reasonable diligence under § 1026.35(c)(4)(vi)(A). This comment is adopted from the proposal without change.

Requirement for two appraisals when sale information is unavailable or conflicting. Under the proposal, a creditor that cannot determine the seller's acquisition date, or a creditor that can determine that the date is within 180 days but cannot determine the price, would have to obtain an additional appraisal before originating a "higher-risk mortgage loan" (now HPML). The proposal included a comment with two examples of how this rule would apply: one in which a creditor is unable to obtain information on the seller's acquisition price or date and the other in which a creditor obtains conflicting information about the seller's acquisition price or date.

Comment 35(c)(4)(vi)(A)-3, discussed further below, gives two examples of how the rule applies. This comment was moved from its placement in the proposal with no substantive change to the requirements of the reasonable diligence standard intended.

Public Comments on the Proposal

The Agencies requested comment on whether 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. The Agencies also requested comment on whether concerns about these potential restraints on credit availability make it particularly important to include the first four source documents listed in the proposed commentary, even though they would be seller-provided, and whether these concerns warrant further expanding the sources of information creditors may rely on to satisfy the reasonable diligence standard under the proposed rule.

The Agencies did not receive comments directly responsive to these questions.

Discussion

In general, the Agencies believe that, based on recent data provided by FHFA discussed in the proposal, most property resales would not trigger the proposal's conditions requiring an additional appraisal.[75] However, the Agencies understand that, in some cases, a creditor performing typical underwriting and documentation procedures may be unable to ascertain through information derived from public records whether the conditions in the additional appraisal requirement have been triggered. For example, a creditor may be unable to determine information about the seller's acquisition because of lag times in recording public records. The Agencies also understand that some source documents often report only estimated amounts of consideration when describing the consideration paid by the current titleholder for the property. Moreover, as noted, several "non-disclosure" jurisdictions do not make the price at which a seller acquired a property publicly available. In addition, the creditor may obtain conflicting information from written source documents. In these cases, a creditor may be unable to determine, based on its reasonable diligence, whether the criteria in § 1026.35(c)(4)(i)(A) and (c)(4)(i)(B) have been met.

Comment 35(c)(4)(vi)(A)-3 provides two examples of how the rule would apply: one in which a creditor is unable to obtain information on the seller's acquisition price or date and the other in which a creditor obtains conflicting information about the seller's acquisition price or date. In the first example, comment 35(c)(4)(vi)(A)-3.i assumes that a creditor orders and reviews the results of a title search showing the seller's acquisition date occurred between 91 and 180 days ago, but the seller's acquisition price was not included. In this case, the creditor would

[75] Based on county recorder information from select counties licensed to FHFA by DataQuick Information Systems.

not be able to determine whether the price the consumer is obligated to pay under the consumer's acquisition agreement exceeded the seller's acquisition price by more than 20 percent. Before extending an HPML subject to the appraisal requirements of § 1026.35(c), the creditor must either: (1) perform additional diligence to obtain information showing the seller's acquisition price and determine whether two written appraisals in compliance with § 1026.35(c)(4) would be required based on that information; or (2) obtain two written appraisals in compliance with § 1026.35(c)(4). This comment also contains a cross-reference to comment 35(c)(4)(vi)(B)-1, which explains the modified requirements for the analysis that must be included in the additional appraisal. *See* § 1026.35(c)(4)(iv); *see also* section-by-section analysis of § 1026.35(c)(4)(vi)(B).

In the second example, comment 35(c)(4)(vi)(A)-3.ii assumes that a creditor reviews the results of a title search indicating that the last recorded purchase was more than 180 days before the consumer's agreement to acquire the property. This comment also assumes that the creditor subsequently receives a written appraisal indicating that the seller acquired the property fewer than 180 days before the consumer's agreement to acquire the property. In this case, unless one of these sources is clearly wrong on its face, the creditor would not be able to determine whether the seller acquired the property within 180 days of the date of the consumer's agreement to acquire the property from the seller, pursuant to § 1026.35(c)(4)(i)(A). Before extending an HPML subject to the appraisal requirements of § 1026.35(c), the creditor must either: (1) perform additional diligence to obtain information confirming the seller's acquisition date (and price, if within 180 days) and determine whether two written appraisals in compliance with § 1026.35(c)(4) would be required based on that information; or (2) obtain two written appraisals in compliance with § 1026.35(c)(4). This comment also contains a cross-reference to comment

35(c)(4)(vi)(B)-1, which explains the modified requirements for the analysis that must be included in the additional appraisal. *See* § 1026.35(c)(4)(iv); *see also* section-by-section analysis of § 1026.35(c)(4)(vi)(B).

As under the proposal, in the final rule, when information about a property is not available from written source documents, creditors extending HPMLs will routinely incur increased costs associated with obtaining the additional appraisal. One risk of this rule is that, because TILA section 129H(b)(2)(B) prohibits creditors from charging their customers for the additional appraisal, creditors will simply refrain from engaging in any HPML where sales history data cannot be obtained. 15 U.S.C. 1639h(b)(2)(B). *See also* § 1026.35(c)(4)(v) (requiring that the creditor cannot charge the consumer for the additional appraisal).

As expressed in the proposal, however, the Agencies believe that requiring an additional appraisal where creditors are unable to obtain the seller's acquisition price and date is necessary to prevent circumvention of the statute. In particular, the Agencies are concerned that not requiring an additional appraisal in cases of limited information may inadequately address the problem of fraudulent property flipping to borrowers of HPMLs in "non-disclosure" jurisdictions, where prior sales data is routinely unavailable through public sources. Similarly, the Agencies are concerned that sellers that acquire and sell properties within a short timeframe could take advantage of delays in the public recording of property sales to engage in fraudulent flipping transactions. The Agencies believe that, where the seller's acquisition date in particular is not in the public record due to recording delays, it is more reasonable to assume that the seller's transaction was sufficiently recent to be covered by the rule than not.

35(c)(4)(vi)(B) Inability to Determine Prior Sale Date or Price – Modified Requirements for Additional Appraisal

Section 35(c)(4)(vi)(B) provides that if, after exercising reasonable diligence, a creditor cannot determine whether the conditions in § 1026.35(c)(4)(i)(A) and (B) are present and therefore must obtain two written appraisals under § 1026.35(c)(4), the additional appraisal must include an analysis of the factors in § 1026.35(c)(4)(iv) (difference in sales price, changes in market conditions, and property improvements) only to the extent that the information necessary for the appraiser to perform the analysis can be determined.

For the reasons discussed above, the Agencies believe that an HPML creditor should be required to obtain an additional appraisal if the creditor cannot determine the seller's acquisition date, or if it can determine the date is within 180 days but cannot determine the price, based on written source documents. However, in keeping with the proposal, § 1026.35(c)(4)(vi)(B) also provides that the additional appraisal in this situation would not have to contain the full analysis required for additional appraisals of flipping transactions under TILA section 129H(b)(2)(A), implemented in the final rule as § 1026.35(c)(4)(iv)(A)-(C). 15 U.S.C. 1639h(b)(2)(A).

Public Comments on the Proposal

The Agencies requested comment on whether an appraiser would be unable to analyze the difference in the price the consumer is obligated to pay to acquire the property and the price at which the seller acquired the property without knowing when the seller acquired the property. If such an analysis is not possible without information about when the seller acquired the property, the Agencies requested comment on whether the rule should assume the seller acquired the property 180 days prior to the date of the consumer's agreement to acquire the property. The Agencies also requested comment generally on the proposed approach to situations in which the creditor cannot obtain the necessary information and whether the rule should address information gaps about the flipping transaction in other ways.

The Agencies did not receive comments directly responsive to these questions.

Discussion

Under the proposal, now adopted in § 1026.35(c)(4)(vi)(B), the additional appraisal must include an analysis of the elements that would be required in proposed § 1026.35(c)(4)(iv)(A)-(C) only to the extent that the creditor knows the seller's purchase price and acquisition date. As discussed in the section-by-section analysis of § 1026.35(c)(4)(iv), TILA section 129H(b)(2)(A) requires that the additional appraisal analyze the difference in sales prices, changes in market conditions, and improvements to the property between the date of the previous sale and the current sale. 15 U.S.C. 1639h(b)(2)(A). An appraiser could not perform this analysis if efforts to obtain the seller's acquisition date and price were not successful.

Consistent with the proposal, comment 35(c)(4)(vi)(B)-1 confirms that, in general, the additional appraisal required under § 1026.35(c)(4)(i) should include an analysis of the factors listed in § 1026.35(c)(4)(iv)(A)-(C). However, the comment also confirms that if, following reasonable diligence, a creditor cannot determine whether the conditions in § 1026.35(c)(4)(i) are present due to a lack of information or conflicting information, the required additional appraisal must include the analyses required under § 1026.35(c)(4)(iv)(A)-(C) only to the extent that the information necessary to perform the analysis is known. As an example, comment 35(c)(4)(vi)(B)-1 assumes that a creditor is able, following reasonable diligence, to determine that the date on which the seller acquired the property occurred between 91 and 180 days prior to the date of the consumer's agreement to acquire the property, but cannot determine the sale price. In this case, the creditor is required to obtain an additional written appraisal that includes an analysis under § 1026.35(c)(4)(iv)(B) and (c)(4)(iv)(C) of the changes in market conditions and any improvements made to the property between the date the seller acquired the property and the date of the consumer's agreement to acquire the property. However, the creditor is not required to obtain an additional written appraisal that includes analysis under § 1026.35(c)(4)(iv)(A) of the difference between the price at which the seller acquired the property and the price that the consumer is obligated to pay to acquire the property.

The Agencies note that the proposed rule does not provide commentary with guidance on the modified requirements for the additional analysis in a situation in which the creditor is unable to determine the date the seller acquired the property but is able to determine the price at which the seller acquired the property. As noted, the Agencies requested but did not receive public comments on this aspect of the proposal. The Agencies are unaware of situations in which the seller's acquisition price, but not the acquisition date, would be known. In the absence of public comment on the issue, the Agencies are not adopting additional guidance on this theoretical situation.

The Agencies believe that allowing creditors to comply with a modified form of the full analysis where a creditor cannot determine information about a property based on its reasonable diligence is a reasonable interpretation of the statute. If a creditor could not determine when or for how much the prior sale occurred, it would be impossible for a creditor to obtain an appraisal that complies with the full analysis requirement of TILA section 129H(b)(2)(A) concerning the change in price, market conditions, and improvements to the property. 15 U.S.C. 1639h(b)(2)(A).

The Agencies' approach to situations in which the creditor cannot obtain the necessary information, either due to a lack of information or conflicting information, can be summed up as follows:

- An additional appraisal is required.

- However, to account for missing or conflicting information, only a modified version of the full additional analysis required under TILA section 129H(b)(2)(A), as implemented by § 1026.35(c)(4)(iv) is required. 15 U.S.C. 1639h(b)(2)(A).

Alternative approaches not chosen by the Agencies include prohibiting creditors from extending the HPML altogether under these circumstances. As stated in the proposal, however, the Agencies believe that a flat prohibition would unduly limit the availability of higher-risk mortgage loans to consumers.

35(c)(4)(vii) Exemptions from the Additional Appraisal Requirement

TILA section 129H(b)(4)(B) permits the Agencies to exempt jointly 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." 15 U.S.C. 1639h(b)(4)(B). The Agencies did not expressly propose any exemptions from the additional appraisal requirement, but invited comment on whether exempting any classes of higher-risk mortgage loans from the additional appraisal requirement (beyond the exemptions in § 1026.35(c)(2)) would be in the public interest and promote the safety and soundness of creditors. The Agencies offered a number of examples of potential exemptions, such as loans made in rural areas, and transactions that are currently exempt from the restrictions on FHA insurance applicable to property resales 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.[76] *See, e.g.*, 24 CFR 203.37a(c). Regarding a possible exemption for

[76] The FHA exceptions to the restrictions on FHA insurance are as follows:
(1) Sales by HUD of Real Estate-Owned (REO) properties under 24 CFR part 291 and of single family assets in revitalization areas pursuant to section 204 of the National Housing Act (12 U.S.C. 1710);
(2) Sales by another agency of the United States Government of REO single family properties pursuant to programs operated by these agencies;

higher-risk mortgage loans (now HPMLs) made in "rural" areas from the additional appraisal requirement, the Agencies requested comment on whether the rule should use the same definition of "rural" that was provided in the 2011 ATR Proposal.[77] This same definition of "rural" was also proposed by the Board regarding Dodd-Frank Act escrow requirements (2011 Escrows Proposal).[78] This definition is reviewed in more detail in the section-by-section analysis of § 1026.35(c)(4)(vii)(H), below.

In the final rule, the Agencies are adopting exemptions from the additional appraisal requirement under § 1026.35(c)(4)(i) for extensions of credit that finance the consumer's acquisition of a property:

(1) From a local, State or Federal government agency (§ 1026.35(c)(4)(vii)(A));

(2) From a person that acquired the property through foreclosure, deed-in-lieu of foreclosure or other similar judicial or non-judicial procedures as a result of exercising the person's rights as a holder of a defaulted mortgage loan (§ 1026.35(c)(4)(vii)(B));

(3) From a non-profit entity as part of a local, State or Federal government program under which the non-profit entity is permitted to acquire single-family properties for resale from a seller who acquired title to the property through the process of foreclosure, deed-in-lieu of foreclosure, or other similar judicial or non-judicial procedure (§ 1026.35(c)(4)(vii)(C));

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(3) Sales of properties by nonprofit organizations approved to purchase HUD REO single family properties at a discount with resale restrictions;
(4) Sales of properties that were acquired by the sellers by inheritance;
(5) Sales of properties purchased by an employer or relocation agency in connection with the relocation of an employee;
(6) Sales of properties by state- and federally-chartered financial institutions and government-sponsored enterprises (GSEs);
(7) Sales of properties by local and state government agencies; and
(8) Only upon announcement by HUD through issuance of a notice, sales of properties located in areas designated by the President as federal disaster areas. The notice will specify how long the exception will be in effect.
24 CFR 203.37a(c).

[77] 76 FR 27390, 28471 (May 11, 2011) (2011 ATR Proposal).

[78] 76 FR 11598, 11612 (March 2, 2011) (2011 Escrows Proposal).

(4) From a person who acquired title to the property by inheritance or pursuant to a court order of dissolution of marriage, civil union, or domestic partnership, or of partition of joint or marital assets to which the seller was a party (§ 1026.35(c)(4)(vii)(D));

(5) From an employer or relocation agency in connection with the relocation of an employee (§ 1026.35(c)(4)(vii)(E));

(6) From a servicemember, as defined in 50 U.S.C. Appx. 511(1), who received deployment or permanent change of station orders after the servicemember acquired the property (§ 1026.35(c)(4)(vii)(G));

(7) Located in an area designated by the President as a federal disaster area, if and for as long as the Federal financial institutions regulatory agencies, as defined in 12 U.S.C. 3350(6), waive the requirements in title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (12 U.S.C. 3331 *et seq.*), and any implementing regulations in that area (§ 1026.35(c)(4)(vii)(F)); and

(8) Located in a "rural" county, as defined in the Bureau's 2013 Escrows Final Rule, § 1026.35(b)(2)(iv)(A) (which is the same definition used in the 2013 ATR Final Rule, § 1026.43(f)(2)(vi) and comment 43(f)(2)(vi-1) (§ 1026.35(c)(4)(vii)(H)).

Public Comments on the Proposal

The Agencies received over fifty comments concerning the questions asked by the Agencies about appropriate exemptions from the additional appraisal requirement. Several commenters opposed requiring two appraisals under any circumstances. However, the Agencies note that the additional appraisal requirement is mandated by statute. TILA section 129H(b)(2), 15 U.S.C. 1639h(b)(2). Commenters in general strongly supported an exemption for loans made in rural areas. The commenters stated that there are limited numbers of licensed and certified appraisers in rural areas, which would make the additional appraisal requirement (requiring appraisals by two independent appraisers) particularly burdensome in these areas. In addition, commenters argued that lenders in rural areas may be forced to hire appraisers from far outside the geographic area, which would increase the time and cost associated with the transaction. Several commenters also stated that rural areas have not historically been sources of fraudulent real estate flipping activity. A number of commenters noted that property prices in rural areas tend to be lower, so the cost of the second appraisal is higher as a percentage of the overall transaction. Two commenters, national trade associations for appraisers, opposed the exemption for rural loans, suggesting that it is not difficult to find two appraisers to value rural properties.

As for how to define "rural," one commenter, a national trade association for community banks, suggested that the agencies use a definition of "rural" that is consistent with the definition used in rules addressing the use of escrow accounts. *See* 2011 Escrows Proposal, discussed below, revised and adopted in the 2013 Escrows Final Rule.[79] Another commenter, a financial holding company, suggested that the final rule exempt lenders located in areas where the State appraiser licensing or certification roster shows five or fewer unaffiliated appraisers within a reasonable distance, such as 50 miles or less. A large bank further recommended that the final rule exempt loans secured by properties in low-density appraiser markets, such as states with fewer than 500 appraisers or counties with fewer than five appraisers.

A large number of commenters also supported an exemption for transactions that are currently exempted from the restrictions on FHA insurance applicable to property resales in the FHA Anti-Flipping Rule. The commenters argued that these categories of transactions do not

[79] *See also* 2011 ATR Proposal at 28471, revised and adopted in the 2013 ATR Final Rule, § 1026.43(f)(2)(vi) and comment 43(f)(2)(vi-1).

present the same risk to consumers and therefore do not require the additional anti-flipping consumer protections.

Two commenters, national trade associations for appraisers, objected to adding any exemptions to the additional appraisal requirement, and suggested that there should be a strong presumption that an additional appraisal is necessary to protect consumers and to promote the safety and soundness of financial institutions.

A number of commenters suggested other exemptions or endorsed exemptions from the entire rule already in the proposal. These are as follows.

- Three commenters (a national trade association for the banking industry, a State trade association for the banking industry, and a bank holding company) suggested an exemption from the second appraisal requirement in cases when the initial appraisal is performed by an appraiser who was selected from the creditor's list of qualified appraisers. The commenters stated that eliminating the seller's ability to influence the selection of the appraiser in this fashion would be sufficient to protect the borrower from the risk of an artificially-inflated appraisal, thereby addressing the fraudulent "flipping" concern the statute seeks to address.
- Two commenters (a nonprofit organization and State credit union association) suggested an exemption for active duty military personnel who receive permanent change of duty station orders.
- A number of commenters (including national trade associations for the mortgage finance and retail banking industry) suggested exemptions for certain non-purchase transactions, such as gifts, transfers in connection with trusts, transfers that do not generate capital gains, and intra-family transfers for estate planning purposes, on

grounds that these transactions are not "profit seeking." Several commenters suggested that transfers in connection with a divorce decree be included in this category as an exemption.

- Many commenters (including two national trade associations for the mortgage finance and retail banking industry, a national trade association for the banking industry, a national trade association for community banks, a national trade association for credit unions, four regional associations for credit unions, a large national bank, a financial holding company, and a community bank) endorsed exemptions for construction and bridge loans, on grounds that these are temporary loans and that consumers are not exposed to risk at the level comparable to other residential loans that Congress targeted in the statute. These commenters also argued that the additional appraisal requirement would be impractical for construction loans, given the inability to conduct interior inspections.
- Two commenters (a community bank and a credit union) suggested an exemption for non-purchase acquisitions and transfers where the consumer previously held a partial interest in the property and cited to Regulation Z (commentary on the definition of residential mortgage transaction) as support.

Discussion

In response to widespread support for adopting exemptions consistent with exemptions from the restrictions on FHA financing in the FHA Anti-Flipping Rule, the Agencies are adopting several exemptions from the additional appraisal requirement generally consistent with exemptions in the FHA Anti-Flipping Rule under 24 CFR 203.37a(c). These are extensions of credit that finance the consumer's acquisition of a property:

- From a local, State or Federal government agency (§ 1026.35(c)(4)(vii)(A); *see also* 24 CFR 203.37a(c)(1), (2) and (7)).
- From an entity that acquired the property through foreclosure, deed-in-lieu of foreclosure or other similar judicial or non-judicial procedures as a result of exercising the person's rights as a holder of a defaulted mortgage loan (§ 1026.35(c)(4)(vii)(B); *see also* 24 CFR 203.37a(c)(6)).
- From a non-profit entity as part of a local, State or Federal government program under which the non-profit entity is permitted to acquire single-family properties for resale from a seller who acquired the property through foreclosure, deed-in-lieu of foreclosure, or other similar judicial or non-judicial procedure (§ 1026.35(c)(4)(vii)(C); *see also* 24 CFR 203.37a(c)(3)).
- From a seller who acquired the property pursuant to a court order of dissolution of marriage, civil union or domestic partnership, or of partition of joint or marital assets to which the seller was a party (§ 1026.35(c)(4)(vii)(D); *see also* 24 CFR 203.37a(c)(4)).
- From an employer or relocation agency in connection with the relocation of an employee (§ 1026.35(c)(4)(vii)(E); *see also* 24 CFR 203.37a(c)(4)).
- Located in an area designated by the President as a federal disaster area, if and for as long as the Federal financial institutions regulatory agencies, as defined in 12 U.S.C. 3350(6), waive the requirements in title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (12 U.S.C. 3331 *et seq.*), and any implementing regulations in that area (§ 1026.35(c)(4)(vii)(F); *see also* 12 CFR 203.37a(c)(4)).

In addition, the Agencies are adopting an exemption for extensions of credit to finance the consumer's purchase of property being sold by a servicemember, as defined in 50 U.S.C. Appx. 511(1), if the servicemember receives deployment or permanent change of station orders after the servicemember purchased the property (§ 1026.35(c)(4)(vii)(G)).

Finally, the Agencies are adopting an exemption for HPMLs in rural areas (§ 1026.35(c)(4)(vii)(H)). The exemption would apply to HPMLs secured by properties in counties considered "rural" under definitions promulgated by the Bureau in the 2013 ATR Final Rule and 2013 Escrows Final Rule – specifically, properties located within the following Urban Influence Codes (UICs), established by the United States Department of Agriculture's Economic Research Services (USDA-ERS): 4, 6, 7, 8, 9, 10, 11, or 12. These UICs generally correspond with areas outside of metropolitan statistical areas (MSAs) and Micropolitan Statistical Areas, defined by the Office of Management and Budget (OMB). For reasons discussed in more detail in the section-by-section analysis of § 1026.35(c)(4)(vii)(H) and the Dodd-Frank Act Section 1022(b)(2) analysis in the **SUPPLEMENTARY INFORMATION** below, rural properties located in micropolitan statistical areas that are not adjacent to an MSA (UIC 8) are also included in the exemption.

Each of these exemptions is discussed in turn below.

35(c)(4)(vii)(A)

Acquisitions of Property from Local, State or Federal Government Agencies

In § 1026.35(c)(4)(vii)(A), the Agencies are adopting an exemption for HPMLs financing consumer acquisitions of property being sold by a local, State or Federal government agency. This exemption generally corresponds with exemptions in the FHA Anti-Flipping Rule for loans financing the purchase of an "REO" (real estate owned) property being sold by HUD or another

U.S. government agency (*see* 12 CFR 203.37a(c)(1) and (2)) and a broad exemption for sales of properties by local and State government agencies (*see* 12 CFR 203.37a(c)(7)). The Agencies do not believe that purchases of properties being sold by local, State or Federal government agencies present the fraudulent flipping risks that the special "higher-risk mortgage" appraisal rules in TILA section 129H were intended to address. 15 U.S.C. 1639h.

Typically, these types of sales are in connection with government programs involving the sale of property obtained through foreclosure or by deed-in-lieu of foreclosure, which can promote affordable housing and neighborhood revitalization. Government agency sales may also be related to foreclosures due to tax liability or related reasons. Without an exemption, most consumer acquisitions involving these types of sales would be subject to the additional appraisal requirement because the government agency typically would have "acquired" the property (for example, in a foreclosure or by deed-in-lieu of foreclosure) for the outstanding balance of the government's lien (plus costs), which is generally less than the value of the property; thus, the price paid to the government agency by the consumer would typically be substantially higher than the government agency's acquisition "price." In addition, these sales might occur relatively soon after the government agency acquired the property, particularly if the acquisition resulted from a foreclosure or tax sale.

The Agencies believe that requiring an HPML creditor to obtain two appraisals to finance transactions involving the purchase of property from government agencies could interfere with beneficial government programs. The Agencies further do not believe that this interference is warranted for these transactions, which do not involve a profit-motivated seller and thus do not present the kinds of flipping concerns that the statute is intended to address. The Agencies believe that an exemption for HPMLs financing the sale of property by a local, State, or Federal government agency is in the public interest because it allows beneficial government programs to go forward as intended. By reducing costs for creditors that might offer HPMLs to finance these transactions, the exemption helps creditors to strengthen and diversify their lending portfolios, thereby promoting the safety and soundness of creditors as well.

35(c)(4)(vii)(B)

Acquisitions of Property Obtained through Foreclosure and Related Means

In § 1026.35(c)(4)(vii)(B), the Agencies are adopting an exemption for HPMLs financing the purchase of a property from a person that had acquired the property through foreclosure, deed-in-lieu of foreclosure, or other similar judicial or non-judicial procedures as a result of exercising the person's rights as a holder of a defaulted mortgage loan. This exemption generally corresponds with an exemption from the FHA Anti-Flipping Rule for loans financing the purchase of properties sold by State- and Federally-chartered financial institutions and GSEs (*see* 12 CFR 203.37a(c)(6)). The Agencies recognize that this exemption might overlap with the exemption in § 1026.35(c)(4)(vii)(A) for sales by government agencies, which might sell properties that the agencies acquire in connection with liquidating a mortgage. However, the Agencies believe that a separate exemption for sales by government agencies is advisable because government agencies might have other reasons for acquiring a property that they then determined was advisable to sell, such as property acquired through exercise of the government's eminent domain powers.

The exemption covers HPMLs that finance the acquisition of a home from a "person" who has acquired title of the property through foreclosure and related means. "Person" is defined in Regulation Z to mean "a natural person or an organization, including a corporation, partnership, proprietorship, association, cooperative, estate, trust, or government unit."

§ 1026.2(a)(22). Thus, consistent with the FHA Anti-Flipping Rule exemptions, the exemption in § 1026.35(c)(4)(vii)(B) covers purchases of properties being sold by State- and Federally-chartered financial institutions, as well as by GSEs such as Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. In addition, the exemption covers HPML loans financing property acquisitions from non-bank mortgage companies, servicers that administer loans held in the portfolios of financial institutions or in pools of mortgages that underlie private and government or GSE asset-backed securitizations, and, less commonly, private individuals. The Agencies believe that a more inclusive exemption for foreclosures better reflects the way that mortgage loans are held and serviced in today's market.

Several commenters pointed out that the sale of REO properties to consumers and potential investors contributes significantly to revitalizing neighborhoods and stabilizing communities. They expressed concerns that the additional appraisal requirement might unduly interfere with these sales, which could have a number of negative effects. First, holders of the mortgages might be forced to hold properties after foreclosure longer than is financially optimal, increasing losses; some public commenters indicated that waiting six months so that the additional appraisal requirement would not apply would be far too long. Second, holders who want or need to clear these properties off of their books might be forced to accept lower prices offered by investors, which would also increase losses. When the holder in this situation is a creditor such as a bank or other financial institution, increased losses can have a negative effect on its safety and soundness. Third, incentives for investors to buy and rehabilitate properties could be reduced, which could be counterproductive to community development and the revitalization of the housing market. Finally, more consumers might have to forego opportunities for homeownership.

For all of these reasons, the Agencies believe that the exemption in § 1026.35(c)(4)(vii)(B) is in the public interest and promotes the safety and soundness of creditors.

35(c)(4)(vii)(C)

Acquisitions of Property from Certain Non-Profit Entities

In § 1026.35(c)(4)(vii)(C), the Agencies are adopting an exemption for HPMLs financing the purchase of a property from a non-profit entity as part of a local, State, or Federal government program under which the non-profit entity is permitted to acquire single-family properties for resale from a seller who acquired the property through foreclosure or similar means. Comment 35(c)(4)(vii)(C)-1 clarifies that, for purposes of 1026.35(c)(4)(vii)(C), a "non-profit entity" refers to a person with a tax exemption ruling or determination letter from the Internal Revenue Service under section 501(c)(3) of the Internal Revenue Code of 1986 (12 U.S.C. 501(c)(3)).[80] This exemption generally builds on an exemption from the FHA Anti-Flipping Rule for loans financing the purchase of properties from nonprofit organizations approved to purchase HUD REO single-family properties at a discount with resale restrictions (*see* 12 CFR 203.37a(c)(3)).

Consistent with the FHA Anti-Flipping Rule exemptions, the exemption in § 1026.35(c)(4)(vii)(C) would cover nonprofit organizations approved to purchase HUD REO single-family properties. In addition, the exemption would cover purchases of these types of properties from nonprofit organizations as part of other local, State or Federal government programs under which the non-profit entity is permitted to acquire title to REO single family properties for resale.

[80] "Person" is defined in Regulation Z as "a natural person or an organization, including a corporation, partnership, proprietorship, association, cooperative, estate, trust, or government unit." § 1026.2(a)(22).

For reasons similar to those discussed under the exemption for loan holders selling a property acquired through liquidating a mortgage (§ 1026.35(c)(4)(vii)(B)), the Agencies believe that the exemption for HPMLs financing the acquisitions described in § 1026.35(c)(4)(vii)(C) is in the public interest and promotes the safety and soundness of creditors. The exemption is intended in part to help holders such as banks and other financial institutions sell properties held as a result of foreclosure or deed-in-lieu of foreclosure, thereby removing them from their books. This can minimize losses, which improves institutions' safety and soundness. The exemption is also intended to facilitate neighborhood revitalization for the benefit of communities and individual consumers. Government programs involving purchases and sales of REO property by non-profits can foster positive community investment and help investors dispense with loss-generating properties efficiently and in a manner that maximizes public benefit. The Agencies do not believe that these types of sales to consumers by non-profits involve serious risks of fraudulent flipping, and thus do not believe that TILA's additional appraisal requirement was intended to apply to these transactions. For these reasons, the Agencies believe that the exemption in § 1026.35(c)(4)(vii)(C) is in the public interest and promotes the safety and soundness of creditors.

35(c)(4)(vii)(D)

Acquisitions from Persons Acquiring the Property through Inheritance or Dissolution of Marriage, Civil Union, or Domestic Partnership

In § 1026.35(c)(4)(vii)(D), the Agencies are adopting an exemption for HPMLs financing the purchase of a property that was acquired by the seller by inheritance or pursuant to a court order of dissolution of marriage, civil union, or domestic partnership, or of partition of joint or marital assets to which the seller was a party. The exemption would include HPMLs financing the acquisition by a joint owner of the property of a residual interest in that property, if the joint owner acquired that interest by inheritance or dissolution of a marriage, civil union, or domestic partnership. This exemption generally corresponds with an exemption from the FHA Anti-Flipping Rule for purchases of properties that had been acquired by the seller by inheritance (*see* 12 CFR 203.37a(c)(4)). As discussed in the section-by-section analysis of § 1026.35(c)(4)(i), above, an exemption for HPMLs that finance the purchase of a property acquired by the seller through a non-purchase transactions was widely supported by commenters.

In response to comments, the Agencies have decided to expand the FHA Anti-Flipping Rule exemption for loans financing the purchase of a property from a seller who had acquired it by inheritance, to include properties acquired as the result of a dissolution of a marriage, civil union, or domestic partnership. The Agencies are not aware that sales of properties so acquired have been the source of fraudulent flipping activity and note that no commenters suggested that this type of flipping occurs. In addition, the Agencies do not believe that Congress intended to cover purchases of property acquired by sellers in this manner with the "higher-risk mortgage" additional appraisal requirement. The Agencies believe that consumer protection from fraudulent flipping is aided by the requirement that the acquisition of property through dissolution of a marriage or civil union must be part of a court order, which can be easily confirmed and helps ensure that the original transfer was for legitimate purposes and not merely to defraud a subsequent purchaser.

As for the exemption for HPMLs financing the purchase of a property acquired by the seller as an inheritance, the Agencies similarly do not see the risk of fraudulent flipping that Congress intended to address occurring in these transactions. Finally, in both the case of inheritance and that of divorce or dissolution, the seller has acquired the property (or full ownership of the property) under adverse circumstances; the Agencies see no reason as a public policy matter to impose further burden on the seller attempting to sell property obtained in this manner. With respect to promoting the safety and soundness of creditors, the Agencies note that a seller attempting to sell property obtained via inheritance or dissolution of marriage may not be in a position to satisfy the mortgage obligation associated with the property. As a result, creditors could be subject to losses, which can negatively affect the safety and soundness of the creditors.

For these reasons, the Agencies believe that the exemptions in § 1026.35(c)(4)(vii)(D) are in the public interest and promote the safety and soundness of creditors.

35(c)(4)(vii)(E)

Acquisitions of Property from Employers or Relocation Agencies

In § 1026.35(c)(4)(vii)(E), the Agencies are adopting an exemption for HPMLs financing the purchase of a property from an employer or relocation agency that had acquired the property in connection with the relocation of an employee. This exemption mirrors an identical exemption from the FHA Anti-Flipping Rule. *See* 12 CFR 203.37a(c)(5)). As with other exemptions adopted in the final rule that correspond with similar FHA Anti-Flipping Rule exemptions, the Agencies concur with FHA's longstanding conclusion that these types of transactions do not present significant fraudulent flipping risks. Rather, the circumstances of the transaction provide evidence that the impetus for the resales stems from bona fide reasons other than the seller's efforts to profit from a flip.

The Agencies believe that these transactions benefit both employees and employers by helping to ensure that employees can relocate as needed for business reasons in an efficient manner. The Agencies also believe that the exemption can benefit HPML consumers and creditors by reducing costs otherwise associated with purchasing and extending credit to finance the purchase of these properties. In addition, due to reduced burden involved with the sale of the home, the Agencies believe the exemption will promote the purchase of homes by employers. This, in turn, promotes the safety and soundness of the employees' creditors by ensuring that the employees' mortgage obligations will be met.

For these reasons, the Agencies believe that the exemption in § 1026.35(c)(4)(vii)(E) is in the public interest and promotes the safety and soundness of creditors.

35(c)(4)(vii)(F)

Acquisitions of Property from Servicemembers with Deployment or Permanent Change of Station Orders

In § 1026.35(c)(4)(vii)(F), the Agencies are adopting an exemption from the additional appraisal requirement for HPMLs financing the purchase of a property being sold by a servicemember, as defined in 50 U.S.C. Appx. 511(1), who received a deployment or permanent change of station order after acquiring the property. This exemption is not in the FHA Anti-Flipping Rule. The exemption was suggested by some commenters in response to a request for recommendations for other appropriate exemptions, however. The Agencies believe that many of the reasons for the exemptions in the final rule based on the FHA Anti-Flipping Rule support a servicemember exemption as well. For example, as with the exemption for HPMLs financing the sale of a property by an employer or relocation agency in connection with the relocation of an employee, the exemption for HPMLs financing the sale of a property by a servicemember with permanent relocation orders facilitates the efficient transfer of servicemembers.

Without this exemption, servicemembers might have more limited options for eligible buyers. For reasons discussed earlier, some creditors might be reticent about lending to an

HPML consumer in a transaction that would trigger the additional appraisal requirement. This could result in servicemembers being forced to retain mortgages that are difficult for them to afford when they must also support themselves and their families in a new living arrangement elsewhere. In turn, the positions of creditors and investors on those existing mortgages could be compromised by servicemembers not being able to meet their mortgage obligations.

The Agencies do not believe that this exemption would be used frequently. Regardless, the Agencies believe that an exemption for HPMLs financing the purchase of the property in that instance is in the public interest and promotes the safety and soundness of creditors.

35(c)(4)(vii)(G)

Acquisitions of a Property in a Federal Disaster Area

In § 1026.35(c)(4)(vii)(G), the Agencies are adopting an exemption for HPMLs financing the purchase of a property located in an area designated by the President as a federal disaster area, if and for as long as the Federal financial institutions regulatory agencies, as defined in 12 U.S.C. 3350(6), waive the requirements in title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (12 U.S.C. 3331 *et seq.*), and any implementing regulations in that area. This exemption generally corresponds to an exemption in the FHA Anti-Flipping Rule for loans financing the purchase of properties located in areas designated by the President as federal disaster areas, if HUD has announced that these transactions will not be subject to the restrictions. *See* 12 CFR 203.37a(c)(8).

The Agencies believe that this exemption appropriately facilitates the repair and restoration of disaster areas to the benefit of individual consumers, communities, and credit markets. The Agencies also recognize that disasters might result in some consumers being unable to meet their mortgage obligations. As a result, creditors could be subject to losses, which could negatively affect the safety and soundness of the creditors. The Agencies believe that this exemption would help creditors extend HPMLs that finance the purchase of properties in disaster areas without undue burden, thus enabling the creditors to improve their lending positions more effectively.

As noted, the Agencies specified that the exemption would take effect only if and for as long as the Federal financial institutions regulatory agencies also waive application of the FIRREA title XI appraisal rules for properties in the disaster area. The Agencies believe that this provision helps protect consumers from fraudulent flipping by giving the Federal financial institutions regulatory agencies, all of which are parties to this final rule, authority to monitor the area and determine when appraisal requirements should be reinstated.

For these reasons, the Agencies have concluded that the exemption in § 1026.35(c)(4)(vii)(G) for the purchase of properties in disaster areas is in the public interest and promotes the safety and soundness of creditors.

35(c)(4)(vii)(H)

Acquisitions of Properties in Rural Counties

In § 1026.35(c)(4)(vii)(H), the Agencies are adopting an exemption from the additional appraisal requirement for HPMLs that finance the purchase of a property in a "rural" county, as defined in § 1026.35(b)(iv)(A), which is a county assigned one of the following Urban Influence Codes (UICs), established by the United States Department of Agriculture's Economic Research Services (USDA-ERS): 4, 6, 7, 8, 9, 10, 11, or 12. These UICs correspond to areas outside of MSAs as well as most micropolitan statistical areas; the definition would also include properties located in micropolitan statistical areas that are not adjacent to an MSA. This rural county exemption is not an exemption in the FHA Anti-Flipping Rule. However, the Agencies received requests to consider an exemption for loans in rural areas during informal outreach for the proposal, as well as from public commenters.

In the proposal, the Agencies did not propose an exemption for loans secured by properties in "rural" areas from all of the Dodd-Frank Act "higher-risk mortgage" appraisal rules, but requested comment on an exemption for these loans from the additional appraisal requirement. As discussed earlier, commenters widely supported an exemption for loans secured by properties in rural areas, citing several reasons: a lack of appraisers; the disproportionate cost of an extra appraisal, based on commenters' view that property values tend to be lower in rural areas than in non-rural areas; the assertion that many lenders in rural areas hold the loans in portfolio and therefore are more mindful of ensuring that properties securing their loans are valued properly; the assertion that lenders in rural areas tend to need to price loans higher for legitimate reasons, so a disproportionate amount of their loans (compared to those of larger lenders) will be subject to the appraisal rules and thus these lenders will bear an unfair burden that they are less equipped than larger lenders to bear; and the assertion that property flipping is rare in rural areas.

The analysis in the proposal of the impact of the proposed rule in rural areas corroborated commenters' concern that a larger share of loans in rural areas tend to be HPMLs than in non-rural areas.[81] Although many small and rural lenders are excluded from HMDA reporting, tabulations of rural loans by HMDA reporters may be informative about patterns of rural HPML usage. As conveyed in the proposal, 10 percent of rural first-lien purchase-money loans were

[81] In the proposal, "rural" was defined as a loan made outside of a micropolitan or metropolitan statistical area. *See* 77 FR 54722, 54752 n. 108 (Sept. 5, 2012).

HPMLs in 2010 compared to 3 percent of non-rural first-lien purchase loans.[82] Based on this information, the Bureau concluded that rural borrowers may be more likely to incur the cost of an additional appraisal requirement than non-rural consumers.

Regarding appraiser availability, analysis conducted for the proposal indicated that more than two appraisers are located in all but 22 counties nationwide (13 of which are in Alaska).[83] An appraiser was considered "located" in a county if the appraiser's home or business address listed on the Appraisal Subcommittee's National Appraiser Registry was in that county. Public commenters pointed out, however, that while many rural areas might have more than two appraisers, these few appraisers are often busy and not readily available. One reason may be that many rural counties cover large areas, perhaps making it more difficult to arrange timely appraisals in such areas. As noted, a financial holding company suggested that the final rule exempt lenders located in areas where the State appraiser licensing or certification roster shows five or fewer unaffiliated appraisers within a reasonable distance, such as 50 miles or less. A large bank further recommended that the final rule exempt loans secured by properties in low-density appraiser markets, such as states with fewer than 500 appraisers or counties with fewer than five appraisers. The final rule does not adopt an exemption based on the number of appraisers within a particular geographic area or radius of the property securing the HPML. The Agencies believe that a simpler approach is consistent with the objectives of the statute, facilitates compliance, and reduces burden on creditors.

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[82] 77 FR 54722, 54752 (Sept. 5, 2012). Similar percentages for rural and non-rural first-lien purchase HPML lending are reflected in 2011 HMDA data. *See* Robert B. Avery, Neil Bhutta, Kenneth B. Brevoort, and Glenn Canner, "The Mortgage Market in 2011: Highlights from the Data Reported under the Home Mortgage Disclosure Act," FR Bulletin, Vol. 98, no. 6 (Dec. 2012) http://www.federalreserve.gov/pubs/bulletin/2012/PDF/2011_HMDA.pdf.

[83] *See* 77 FR 54722, 54752-54753 (Sept. 5, 2012).

Other than the commenters who suggested a "radius" or low-density approach for the rural exemption, only one other commenter offered suggestions on how to define rural. This commenter recommended that the Agencies adopt a definition of "rural" that is consistent with the definition used in rules addressing the use of escrow accounts. *See* 2013 Escrows Final Rule, § 1026.35(b)(2)(iv); *see also* 2013 ATR Final Rule, § 1026.43(f)(2)(vi) and comment 43(f)(2)(vi-1). The Agencies specifically requested comment on whether the definition of "rural" used in any exemption adopted should be the same as the definition in the 2011 ATR Proposal and 2011 Escrows Proposal. These exemptions are described below.

2011 Escrows Proposal. Since 2010, Regulation Z, implementing TILA, has required creditors to establish escrow accounts for taxes and insurance on HPMLs. *See* 12 CFR 1026.35(b)(3). The Dodd-Frank Act subsequently amended TILA to codify and augment the escrow requirements in Regulation Z. *See* Dodd-Frank Act §§ 1461 and 1462, adding 15 U.S.C. 1639d. The Board issued the 2011 Escrows Proposal to implement a number of these provisions.

Among other amendments, one new section of TILA authorizes the Board (now, the Bureau) to create an exemption from the requirement to establish escrow accounts for transactions originated by creditors meeting certain criteria, including that the creditor "operates predominantly in rural or underserved areas." 15 U.S.C. 1639d(c).

Accordingly, the 2011 Escrows Proposal proposed to create an exemption for any loan extended by a creditor that makes most of its first-lien HPMLs in counties designated by the Board as "rural or underserved," has annual originations of 100 or fewer first-lien mortgage loans, and does not escrow for any mortgage transaction it services.

Definition of "Rural"

In the 2011 Escrows Proposal, the Board proposed to define “area” as “county” and to provide that a county would be designated as “rural” during a calendar year if:

> . . . it is not in a metropolitan statistical area or a micropolitan statistical area, as those terms are defined by the U.S. Office of Management and Budget, and either (1) it is not adjacent to any metropolitan or micropolitan area; or (2) it is adjacent to a metropolitan area with fewer than one million residents or adjacent to a micropolitan area, and it contains no town with 2,500 or more residents.

See 76 FR 11598, 11610-13 (March 2, 2011); proposed 12 CFR § 1026.45(b)(2)(iv)(A).

Further, the Board proposed to clarify in Official Staff Commentary to this provision that, on an annual basis, the Board would “determine[] whether each county is ‘rural’ by reference to the currently applicable Urban Influence Codes (UICs), established by the United States Department of Agriculture’s Economic Research Service (USDA-ERS). Specifically the Board classifies a county as “rural” if the USDA-ERS categorizes the county under UIC 7, 10, 11, or 12.” *See* proposed comment 45(b)(2)(iv)-1.

The Board explained its proposed definition of “rural” in the **SUPPLEMENTARY INFORMATION** to the proposal as follows:

> The Board is proposing to limit the definition of ‘‘rural’’ areas to those areas most likely to have only limited sources of mortgage credit. The test for ‘‘rural’’ in proposed § 226.45(b)(2)(iv)(A), described above, is 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. The ERS devised the urban influence codes to reflect such

> factors as counties' relative population sizes, degrees of ''urbanization,'' access to larger communities, and commuting patterns. The four codes captured in the proposed ''rural'' definition represent the most remote rural areas, where ready access to the resources of larger, more urban communities and mobility are most limited. Proposed comment 45(b)(2)(iv)–1 would state that the Board classifies a county as ''rural'' if it is categorized under ERS urban influence code 7, 10, 11, or 12.

Id. at 11612.

2011 ATR Proposal. The Dodd-Frank Act also amended TILA to impose new requirements that creditors consider a consumer's ability to repay a mortgage loan secured by the consumer's principal dwelling. *See* Dodd-Frank Act § 1411, adding 15 U.S.C. 1639c. As part of these amendments, the Dodd-Frank Act created a new class of loans called "qualified mortgages" and provided that creditors making qualified mortgages would be presumed to have met the new ability to repay requirements. *See id.* § 1412. Under the Act, balloon mortgages can be considered qualified mortgages if they meet certain criteria, including that the creditor "operates predominantly in rural or underserved areas." *Id.*

In May 2011, the Board issued the 2011 ATR Proposal to implement these provisions. In the ATR Proposal, the Board's proposed definition of "rural" and accompanying explanation in the Official Staff Commentary and **SUPPLEMENTARY INFORMATION** are identical to the definition and explanation quoted above in the 2011 Escrows Proposal. *See* 76 FR 27390, 27469-72 (May 11, 2011); proposed § 1026.43(f)(2)(i) and comment 43(f)(2)-1.

As discussed in more detail in the 2013 ATR Final Rule and 2013 Escrows Final Rule, most commenters on the proposals for those rulemakings objected to this definition of "rural" as too narrow (it covers approximately 2 percent of the U.S. population). The narrow scope of the definition of "rural" was viewed as especially onerous because the scope was narrowed even further by a number of additional conditions on the exemption imposed by the statute.[84] As explained more fully in the 2013 ATR Final Rule and 2013 Escrows Final Rule, the Bureau is finalizing a more broad definition of "rural," acknowledging that the exemption will nonetheless be narrowed by the additional conditions.

The Bureau is defining "rural" as UICs 4, 6, 7, 8, 9, 10, 11, or 12. These codes comprise all areas outside of MSAs and outside of all micropolitan statistical areas except micropolitan statistical areas that are not adjacent to MSAs. According to current U.S. Census data, approximately 10 percent of the U.S. population lives in these areas.

Exemption for HPMLs secured by properties in rural counties from the additional appraisal requirement. The Agencies believe that the definition of "rural" county used by the Bureau is appropriate for the exemption from the requirement to obtain an additional appraisal under § 1026.35(c)(4)(i) for loans in rural areas. In addition, the Agencies view consistency across mortgage rules in defining rural county as desirable for compliance and enforcement. Thus, the exemption in § 1026.35(c)(4)(vii)(H) cross-references the definition of rural county in the HPML escrow provisions of revised § 1026.35(b) (*see* 2013 Escrows Final Rule, § 1026.35(b)(2)(iv)). (The same definition of rural county is adopted by the Bureau in the 2013

[84] For the exemption from the escrow requirement, the statute states that the Board (now, the Bureau) may exempt a creditor that: "(1) operates predominantly in rural or underserved areas; (2) together with all affiliates, has total annual mortgage loan originations that do not exceed a limit set by the [Bureau]; (3) retains its mortgage loan originations in portfolio; and (4) meets any asset size threshold and any other criteria the [Bureau] may establish . . . ." TILA section 129D(c), 15 U.S.C. 1639d(c); *see also* TILA section 129C(b)(2)(E), 15 U.S.C. 1639c(b)(2)(E) (granting the Bureau authority to deem balloon loans "qualified mortgages" under certain circumstances, including that the loan is extended by a creditor described meeting the same conditions set forth for the exemption from the escrow requirement).

ATR Final rule, § 1026.43(f)(2)(vi) and comment 43(f)(2)(vi-1).) The Agencies have considered several factors in determining how to define the scope of the exemption.

First, the Agencies believe that creditors must be readily able to determine whether a particular transaction qualifies for the exemption. This will be possible because the Bureau will annually publish on its website a table of the counties in which properties would qualify for this exemption. Comment 35(c)(4)(vii)(H)-1 cross-references comment 35(b)(2)(iv)-1, which clarifies that the Bureau will publish on its website the applicable table of counties for each calendar year by the end of that calendar year. The comment further clarifies that a property securing an HPML subject to § 1026.35(c) is in a rural county under § 1026(c)(4)(vii)(H) if the county in which the property is located is on the table of rural counties most recently published by the Bureau. The comment provides the following example: for a transaction occurring in 2015, assume that the Bureau most recently published a table of rural counties at the end of 2014. The property securing the transaction would be located in a rural county for purposes of § 1026(c)(4)(vii)(H) if the county is on the table of rural counties published by the Bureau at the end of 2014. The Agencies anticipate that loan officers and others will be able to look on the Bureau website to identify whether the county in which the subject property is located is on the list.

Second, the Agencies endeavored to create an exemption tailored to address key concerns raised by commenters requesting a rural exemption, based on data findings by the Agencies. The principal concerns that the Agencies identified among commenters were that: first, adequate numbers of appraisers might not be available in rural areas for creditors to comply with the additional appraisal requirement and; second, the cost of obtaining the additional appraisal might deter some creditors from making HPMLs in these areas, many of which might already be underserved, reducing credit access for rural consumers. As noted in the proposed rule and discussed below, the potential reduction in credit access might be disproportionally greater in rural areas than in non-rural areas because the proportion of HPMLs is higher in rural as opposed to non-rural areas.

For the reasons explained below, the Agencies believe that the exemption for loans in rural areas as defined in the final rule is appropriately tailored to address these and related concerns. By better ensuring credit access and lowering costs among creditors extending HPMLs in rural areas, including small community banks, the exemption is expected to benefit the public and promote the safety and soundness of creditors. *See* TILA section 129H(b)(4)(B), 15 U.S.C. § 1639h(b)(4)(B).

Appraiser availability. As noted, commenters indicated that in some rural areas it can be difficult to find appraisers who are both competent to appraise a particular rural property and also readily available. The cost-benefit analysis conducted by the Bureau for the proposal focused in part on estimating appraiser availability in particular areas and identified counties in which fewer than two appraisers with requisite credentials indicated having a business or home address.[85]**SUPPLEMENTARY INFORMATION** However, commenters noted and the Agencies confirmed based on additional outreach for this final rule that not all appraisers whose home or business address is in a particular geographic area are competent to appraise properties in that area. Thus, to inform the final rule, the Bureau expanded its research from that conducted for the proposal.

For the final rule, the Bureau computed how many appraisers showed that they had a home or business address within a 50-mile radius of the center of each census tract in which an

[85] *See* 77 FR 54722, 54752-54753 (Sept. 5, 2012).

HPML loan was reported in the 2011 HMDA data.[86] The 50-mile radius test was intended to be a proxy for the potential service area for an appraiser in a more rural area and would cover properties located in roughly an hour's drive of an appraiser's home or office location.

On this basis, the Bureau found that, of 262,989 HMDA-reported HPMLs in 2011, 603 had fewer than five appraisers within a 50-mile radius of the center of the tract in which the securing property was located; 484 of these loans were in areas covered by the final rule's rural exclusion. Based on FHFA data, the Bureau estimates that 5 percent of these HPMLs were potentially covered by the statute's additional appraisal requirement because they were purchase-money HPMLs secured by properties sold within a 180-day window.[87] A lower proportion would have been flips with a price increase. *See* TILA section 129H(b)(2)(A), 15 U.S.C. 1639h(b)(2)(A). But taking solely the number of flips without regard to price increase or other exemptions (*see* § 1026.35(c)(2) and (c)(4)(vii)), an estimated 30 HPML transactions that were flips had fewer than five appraisers within a 50-mile radius of the center of the census tract in which they were located (5 percent of 603 HPMLs). Twenty-four of these would have been covered by the rural exemption as defined in the final rule (5 percent of 484 HPMLs).

On this basis, the Agencies have concluded that the exemption is reasonably tailored to exclude from coverage of the additional appraisal requirement the loans for which appraiser availability might be an issue.

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[86] The appraisers accounted for in the Bureau's analysis of the National Appraiser Registry were listed on the Registry as "active," "AQB Compliant" and either licensed or certified. The Registry is available at https://www.asc.gov/National-Registry/NationalRegistry.aspx. "AQB Compliant" means that the appraiser met the Real Property Appraisal Qualification Criteria as promulgated by the Appraisal Qualifications Board on education, experience, and examination. *See* Appraisal Subcommittee of the Federal Financial Institutions Examination Council, https://www.asc.gov/Frequently-Asked-Questions/FrequentlyAskedQuestions.aspx#AQB%20Compliant%20meaning.

[87] Based on county recorder information from select counties licensed to FHFA by DataQuick Information Systems.

Credit access. Commenters also raised concerns about credit access, emphasizing that a larger proportion of loans in rural areas are HPMLs than in non-rural areas. Commenters suggested that the additional appraisal requirement could deter some creditors from extending HPML credit. *See* § 1026.35(c)(4)(v) and corresponding section-by-section analysis.

The additional appraisal requirement entails several compliance steps. After identifying that a loan is an HPML under § 1026.35(a), a creditor will need to assess whether the HPML is exempt from the appraisal requirements entirely under § 1026.35(c)(2). If the loan is not exempt as a qualified mortgage or other type of transaction exempt under § 1026.35(c)(2), the creditor will need to determine whether the HPML is one of the transactions that is exempt from the additional appraisal requirement under § 1026.35(c)(4)(vii). If the HPML is not exempt from the additional appraisal requirement, the creditor will need to determine whether the requirement to obtain an additional appraisal is triggered based on the date and, if necessary, price of the seller's acquisition of the property securing the HPML. *See* § 1026.35(c)(4)(i)(A) and (B). (Alternatively, the creditor could assume that the requirement applies and order two appraisals without taking each of these steps.) If the requirement is triggered, the creditor must obtain an additional appraisal performed by a certified or licensed appraiser, the cost of which cannot be charged to the consumer. *See id.* and § 1026.35(c)(4)(v).

If these compliance obligations would deter some creditors from extending HPMLs, the impact on credit access might be greater in rural areas as defined in the final rule than in non-rural areas, because a significantly larger proportion of residential mortgage loans made in rural areas are HPMLs than in non-rural areas. Again, based on 2011 HMDA data, 12 percent of rural first-lien, purchase-money loans were HPMLs compared to four percent of non-rural first-lien, purchase-money loan.[88] That is, recent data indicates that HPMLs occur three times as often in the rural setting.

Thus, an important consideration for the Agencies in determining the scope of the exemption was the comparative number of creditors extending HPMLs in various geographic areas. To this end, the Agencies considered, based on HMDA data, the number of creditors reported to have extended HPML credit in the geographic units defined by the 12 UICs. (For more details, see the Section 1022(b)(2) cost-benefit analysis in the **SUPPLEMENTARY INFORMATION** below.) The Agencies believe that in the areas with a greater number of lenders reporting that they extended HPMLs, the additional appraisal requirement will have a lower impact on credit access.

HMDA data for 2011 show that a sharp drop-off in the number of creditors reporting to extend HPML credit occurs in micropolitan statistical areas not adjacent to MSAs (UIC 8), compared to MSAs and micropolitan statistical areas that are adjacent to MSAs.[89] Specifically, 10 creditors reported that they extended HPMLs in a median county classified as UIC 8 in 2011; by contrast, in the median counties of the UICs with the next highest populations (UICs 2, 3, 5), the number of creditors reporting that they extended HPMLs was 24, 18, and 16, respectively. The drop-off in numbers of HPML creditors continues for UICs representing non-MSAs and non-micropolitan statistical areas.[90]

The Agencies also looked at the estimated number of flips in areas encompassed by the rural exemption of the final rule to determine whether the consumer protections lost might

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[88] Robert B. Avery, Neil Bhutta, Kenneth B. Brevoort, and Glenn Canner, "The Mortgage Market in 2011: Highlights from the Data Reported under the Home Mortgage Disclosure Act," FR Bulletin, Vol. 98, no. 6 (Dec. 2012) http://www.federalreserve.gov/pubs/bulletin/2012/PDF/2011_HMDA.pdf.

[89] More detail about the population densities represented by the 12 UICs is provided in the Section 1022(b)(2) analysis in Part V of the **SUPPLEMENTARY INFORMATION**.

[90] Ten creditors reported extending HPML credit in 2011 in UICs 6 and 4; six in UIC 11; seven in UIC 9; six in UIC 7; four in UIC 10; and three in UIC 12.

outweigh the benefits of the exemption. As explained in greater detail in the Section 1022(b)(2) analysis, the Bureau estimates that, based on HMDA data, 122,806 purchase-money HPMLs were made in 2011; 21,370 of those were in the areas covered by the rural exclusion. As noted, the Bureau estimates that the proportion of purchase-money HPMLs involving properties sold within 180 days is 5 percent.[91] Thus, of HPMLs in rural counties as defined in the final rule, an estimated 5 percent would have been flips. This number does not account for any other exemptions from the HPML appraisal rules that might apply to these HPMLs under § 1026.35(c)(2) or (c)(4)(vii). It also does not account for the price increase thresholds defining a transaction covered under the additional appraisal requirement in this final rule. *See* § 1026.35(c)(4)(i)(A) and (B) and corresponding section-by-section analysis.

The Agencies believe that the exemption for HPMLs secured by rural properties appropriately balances credit access and consumer protection. As the data above suggests, the estimated number of HPML consumers that would not receive the protections of an additional appraisal due to this exemption is very small. Moreover, the Agencies note that affected HPML consumers would still receive the consumer protections afforded by the general requirement for an interior-inspection appraisal performed by a certified or licensed appraiser. *See* § 1026.35(c)(3)(i).

In sum, the Agencies believe that the exemption in § 1026.35(c)(4)(vii)(G) will help ensure that creditors in rural areas are able to extend HPML credit without undue burden, which will in turn mitigate any detrimental impacts on access to credit in rural areas that might result absent the exemption. The Agencies further believe that the exemption is appropriately tailored to ensure that needed consumer protections regarding appraisals are in place in areas where they

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[91] Based on county recorder information from select counties licensed to FHFA by DataQuick Information Systems.

are needed. For all of the reasons explained above, the Agencies have concluded that the exemption in § 1026.35(c)(4)(vii)(H) is in the public interest and promotes the safety and soundness of creditors.

35(c)(5) Required Disclosure

35(c)(5)(i) In General

Title XIV of the Dodd-Frank Act added two new appraisal-related notification requirements for consumers. First, TILA section 129H(d) states that, at the time of the initial mortgage application for a higher-risk mortgage loan, the applicant shall be "provided with a statement by the creditor that any appraisal prepared for the mortgage is for the sole use of the creditor, and that the applicant may choose to have a separate appraisal conducted at the expense of the applicant." 15 U.S.C. 1639h(d). The Agencies interpret TILA section 129H(d) to provide the elements that a disclosure imposed by regulation should address. In addition, new section 701(e)(5) of the Equal Credit Opportunity Act (ECOA) similarly requires a creditor to notify an applicant in writing, at the time of application, of the "right to receive a copy of each written appraisal and valuation" subject to ECOA section 701(e). 15 U.S.C. 1691(e)(5); *see also* 77 FR 50390 (Aug. 21, 2012) (2012 ECOA Appraisals Proposal) and the Bureau's final ECOA appraisals rule (2013 ECOA Appraisals Final Rule).[92] Read together, the revisions to TILA and ECOA require creditors to provide two appraisal disclosures to consumers applying for a higher-risk mortgage loan secured by a first lien on a consumer's principal dwelling.

The Agencies proposed text for the notice required by TILA section 129H that was intended to incorporate the statutory elements, using language honed through consumer testing designed to minimize confusion both with respect to the language on its face, as well as when

[92] The Bureau released the 2013 ECOA Appraisals Final Rule on January 18, 2013, under Docket No. CFPB-2012-0032, RIN 3170-AA26, at http://consumerfinance.gov/Regulations.

read in conjunction with appraisal notices required under the ECOA. Under the proposal, the TILA section 129H notice stated: "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."

As explained more fully below, in § 1026.35(c)(5), the Agencies are adopting the proposed disclosure provision with one change – in effect, including the word "promptly" in the disclosure is optional.

Public Comments on the Proposal

The Agencies received approximately 20 comments pertaining to the proposal on the text, timing, and form of the HRM appraisal notice. The comments came from banks and bank holding companies, credit unions, bank and credit union trade associations, an appraisal industry trade association, GSEs, consumer advocates, and an industry service provider. Regarding the text of the disclosure, the Agencies requested comment on the proposed language and whether additional changes should be made to the language to further enhance consumer comprehension.

Combining ECOA/TILA notices. A bank and service provider commented that the proposed text was clear and easy to understand. A major bank, a credit union trade association, and GSEs supported the proposal to streamline and integrate the ECOA appraisal notice and the TILA appraisal notice into a single notice. The credit union trade association noted this harmonization would increase the likelihood consumers would read and understand the notice. No commenters objected to the integration of the ECOA and TILA notices.

Use of "promptly" for the timing of disclosure of appraisals. Several commenters – a bank and two bank trade associations at the State level – expressed concern that the term "promptly" in the proposed notice was not defined, and that the failure to define the term could lead to consumer confusion as well as disputes. One commenter suggested that the term "promptly" be defined as within three days before closing, which the commenter indicated would be consistent with Regulation B.

Use of the term "appraisal," without reference to "valuations." A major bank suggested that the term "valuations" should be added to the text of the notice, because disclosure of valuations also is required by ECOA (and the 2012 ECOA Appraisals Proposal, finalized in the 2013 ECOA Appraisals Final Rule). Because consumers may be unfamiliar with the term "valuation," the bank also suggested that the notice include a list of documents that constitute a "valuation," and several other statements regarding how valuations may be conducted and used by the lender. A GSE also suggested that the term "valuations" appear in the notice, so that when copies of valuations are provided under ECOA consumers would not mistake them for appraisals.

Statement that the appraisal will be provided even if the loan does not close. A bank trade association at the State level commented on the part of the notice stating that the appraisal would be provided "even if your loan does not close." The commenter suggested that consumers need to be informed that the creditor is not "compelled to order an appraisal if it is determined that the loan will not be consummated prior to appraisal order process." This commenter suggested adding the qualifier, "if an appraisal was obtained."

Ability of creditor to levy certain charges. One bank commenter expressed concern that the proposed notice did not condition the right of the borrower to receive a copy of the appraisal upon the borrower's payment for the appraisal. A credit union trade association suggested that the notice clarify that the borrower may be charged for any “additional copies” of the appraisal that are requested by the borrower.

Potential for consumer expectations regarding creditor use of the applicant-ordered appraisal. Several commenters – national and State banking trade associations, a major credit union trade association, and an appraisal industry trade association – expressed concern over the text informing the applicant of the applicant’s right to order his or her own appraisal for his or her own use. These commenters noted that the proposed notice did not clearly state what use, if any, a creditor could make of a borrower-ordered appraisal.

- Three commenters suggested that the notice clarify that the borrower-ordered appraisal would not be used by the creditor. One of these commenters stated that Federal guidelines prohibited use of the borrower-ordered appraisal as the appraisal for the transaction. The bank trade associations argued that the creditor is prohibited by law from “considering” the borrower-ordered appraisal (pointing, for example, to the Appraisal and Evaluation Interagency Guidelines[93]). Similarly, a national credit union trade association suggested that the notice clarify that a borrower-ordered appraisal “will not be taken into consideration.”
- By contrast, another State bank trade association suggested a less categorical clarification, that the lender “has no obligation to use or review any borrower-ordered appraisal.”

Discussion

Section 1026.35(c)(5) of the final rule provides that, unless an exemption from the

[93] The Interagency Guidelines state: “An institution’s use of a borrower-ordered or borrower-provided appraisal violates the [FIRREA title XI] appraisal regulations. However, a borrower can inform an institution that a current appraisal exists, and the institution may request it directly from the other financial services institution.” 75 FR 77450, 77458 (Dec. 10, 2010).

HPML appraisal rules applies under § 1026.35(c)(2) (discussed in the corresponding section-by-section analysis above), a creditor shall disclose the following statement, in writing, to a consumer who applies for an HPML: "We may order an appraisal to determine the property's value and charge you for this appraisal. We will 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." Section 1026.35(c)(5) further provides that compliance with the disclosure requirement in Regulation B, 12 CFR § 1002.14(a)(2) satisfies the requirements of this paragraph. Under § 1026.35(c)(5)(ii) in the final rule, this disclosure shall be delivered or placed in the mail no later than the third business day after the creditor receives the consumer's application for a higher-priced mortgage loan subject to § 1026.35(c). In the case of a loan that is not a higher-priced mortgage loan subject to § 1026.35(c) at the time of application, but becomes a higher-priced mortgage loan subject to § 1026.35(c) after application, the disclosure shall be delivered or placed in the mail not later than the third business day after the creditor determines that the loan is a higher-priced mortgage loan subject to § 1026.35(c).

Combining ECOA/TILA notices. As noted, there was strong industry support for harmonizing the ECOA/TILA notice language. Consumer testing also supported this harmonization, as discussed in the proposal. The Agencies therefore retain the proposed approach of harmonizing the TILA appraisal notice with language for the ECOA notice.

Use of "promptly" for the timing of disclosure of appraisals. The Agencies have decided to give creditors the option of providing the HPML appraisal disclosure with or without the word "promptly." Specifically, the final rule clarifies that a creditor may comply with the HPML appraisal disclosure requirement – which does not incorporate "promptly" – by providing the disclosure required under ECOA's Regulation B, which does. Indeed, this is the only difference between the two notices. The model language for the Bureau's final rule implementing ECOA's appraisal disclosure requirement in Regulation B incorporates "promptly" to conform to statutory language in ECOA. *See* ECOA section 701(e)(1), 15 U.S.C. 1691(e)(1); *see also* 2013 ECOA Appraisals Final Rule, 12 CFR 1002, App. C (model form C-9). Specifically, ECOA requires that a creditor of a first-lien dwelling-secured mortgage provide the applicant with a copy of each written appraisal and other valuation "promptly, and in no case later than three days prior to closing of the loan, whether the creditor grants or denies the applicant's request for credit or the application is incomplete or withdrawn." ECOA section 701(e)(1), 15 U.S.C. 1691(e)(1). TILA's "higher-risk mortgage" appraisal requirements in section 129H(c) do not use the word "promptly" in describing the timing requirement for creditors to provide a copy of the appraisal. Instead, the timing requirement is defined only as "at least 3 days prior to the transaction closing date." 15 U.S.C. 1639h(c).

In the final rule, the Agencies are not requiring HPML creditors to include "promptly" in the HPML appraisal notice under § 1026(c)(5)(i) because "promptly" is not the legal standard for providing a copy of the appraisal in TILA section 129H(c). 15 U.S.C. 1639h(c).

At the same time, the Agencies recognize that all first-lien dwelling-secured mortgages, including first-lien HPMLs, are subject to the ECOA disclosure and appraisal copy requirements. Therefore, under the final rule, first-lien HPML creditors who wish to provide a single notice to comply with both TILA and ECOA can do so by using the ECOA notice with the word "promptly" into the disclosure. Subordinate-lien HPMLs are subject only to TILA's rules on appraisal copies, not ECOA's, so the timing requirement of "promptly" does not apply to creditors of subordinate-lien HPMLs. Therefore, under the final rule, subordinate-lien HPML creditors have the option of providing a disclosure without the word "promptly;" however, the final rule also makes it clear that any creditor, whether of a first- or subordinate-lien HPML, complies with the HPML appraisal disclosure requirement by complying with the disclosure requirement under ECOA's Regulation B. As noted, the model language for the ECOA/Regulation B disclosure includes the word "promptly."

Use of term "appraisal," without reference to "valuations." For several reasons, the Agencies have decided to retain the term "appraisal" in the disclosure notice and not refer to "valuations." First, the duty to disclose valuations in addition to appraisals arises under ECOA, not TILA. The Bureau sought comment on the issue in its proposed ECOA appraisal rule and is not requiring the use of the term "valuation" in its final version of that rule. *See* 77 FR 50390, 50396 (Aug. 21, 2012); 2013 ECOA Appraisals Final Rule § 1002.14(a)(1) and appendix C, Form C-9. The Agencies do not believe that the issue is appropriately addressed in a rule implementing the TILA requirement expressly relating only to "appraisals."

The Agencies also note that, as discussed more fully in the Bureau's 2013 ECOA Appraisals Final Rule, consumer comprehension would not necessarily be enhanced by use of the term "valuation." In consumer testing by the Bureau, for example, a settlement statement whose "appraisal" section did not refer to valuations generally was viewed as less confusing than one that did refer to valuations. Including the term "valuations" in the HPML appraisal notice also might confuse subordinate-lien borrowers and creditors, because neither TILA nor ECOA requires disclosure of valuations for subordinate-lien loans.

Statement that the appraisal will be provided even if the loan does not close. The Agencies are retaining the proposed language that the consumer will receive a copy of the appraisal "even if your loan does not close." This reflects the statutory requirement of providing a copy of each appraisal "conducted," a requirement the Agencies interpret as applying whether or not the loan ultimately is consummated. TILA section 129H(c) and (d), 15 U.S.C. 1639h(c) and (d).

The Agencies decline to add a qualifier suggested in public comments explaining that the creditor might not order an appraisal if the creditor determines that the applicant will not qualify for a loan before the appraisal is ordered. The Agencies do not believe that this clarification, while true, is necessary for the disclosure. The proposed notice, now adopted, states that the creditor "may" order an appraisal. This language indicates that the creditor is not always required to order an appraisal. Further, the proposed text, now adopted, states that the creditor will provide a copy of "any appraisal." This additional language also underscores the possibility that in some situations (such as if the loan will not close), an appraisal might not be ordered.

Ability of creditor to levy certain charges. The Agencies decline to add language to the disclosure indicating that the consumer's right to receive a copy of the appraisal is conditioned on payment for the appraisal. TILA does not condition the consumer's right to receive a copy of each appraisal in an HPML transaction on payment for the appraisal. *See* TILA section 129H(c), 15 U.S.C. 1639h(c). Moreover, a statement to this effect would directly contradict the statutory prohibition against charging for any second appraisal required by the HPML appraisal rule. *See* TILA section 129H(b)(2)(B), 15 U.S.C. 1639h(b)(2)(B), implemented in § 1026.35(c)(4)(v), discussed above. Such a statement would also further complicate the disclosure, potentially increasing consumer confusion. Regarding whether a creditor may condition the consumer's right to receive a copy of an appraisal for a first-lien HPML transaction that is also subject to

ECOA, the Agencies believe that the issue is more properly addressed in the 2013 ECOA Appraisals Final Rule.[94]

The Agencies also decline to revise the appraisal notice to state that the creditor may charge the consumer for additional copies. The proposed notice, as adopted, refers to the obligation to provide "a copy," singular. Consumer testing did not suggest consumers were likely to believe that they had a right to multiple free copies, and it is unclear that borrowers frequently or even regularly request multiple copies of the appraisals. The Agencies believe that consumer understanding is best enhanced by keeping the disclosure as simple as possible, in part by excluding nonessential information.

Potential for consumer expectations regarding creditor use of a borrower-ordered appraisal. The proposed disclosure stated: "You can pay for an additional appraisal for your own use at your own cost." As noted, several commenters expressed concerns that this statement might create misunderstandings about whether the creditor has an obligation to consider an appraisal ordered by a consumer. Some commenters suggested additional language to address the issue.

The Agencies are not adopting additional language for the disclosure on this issue. Consumer testing on iterations of the disclosure language did not indicate that the proposed notice would mislead borrowers into believing that creditors are required to consider borrower-ordered appraisals. The language concerning use of a borrower-ordered appraisal evolved during the consumer testing, to reduce confusion. One version of language the Bureau tested contained no suggestion as to the use of borrower-ordered appraisals: "You can choose to pay for your own

[94] Regulation B currently does not require a creditor to provide an appraisal before the borrower pays for it. 12 CFR 1002.14(a)(2)(ii). The Bureau's 2012 ECOA Appraisals Proposal would have eliminated this aspect of Regulation B, however. *See* 77 FR 50390, 50403 (Aug. 21, 2012). The Bureau adopted this change in the 2013 ECOA Appraisals Final Rule. *See* new § 1002.14(a)(1).

appraisal of the property."[95] Consumers participating in the testing had difficulty understanding the purpose of this language; moreover, industry testing participants noted a concern that consumers might take it to mean that the consumer could order the consumer's own appraisal to be used by the creditor in lieu of the creditor-ordered appraisal.[96] The Bureau subsequently modified the language to add the "for your own use" language,[97] and this is the language the Agencies proposed. The Agencies believe that the phrase, "for your own use," is succinct and enhances consumer understanding that an appraisal ordered by the consumer is not a substitute for the appraisal ordered by the creditor.

In addition, the Agencies do not wish to include language in a disclosure that might inadvertently discourage consumers from questioning the appraisal report ordered by the creditor and providing the creditor with any supporting information that may be relevant to the question of the property's value.

The Agencies also recognize that creditors are subject to existing Federal regulatory and supervisory regulations and requirements that provide additional guidance to creditors about appropriate and inappropriate use of borrower-ordered appraisals. To affirm these existing requirements, the final rule states in comment 35(c)(5)(i)-2 that nothing in the text of the consumer notice required by § 1026.35(c)(5) should be construed to affect, modify, limit, or supersede the operation of any legal, regulatory, or other requirements or standards relating to independence in the conduct of appraisers or the prohibitions against use of borrower-ordered appraisals by creditors.

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[95] Kleimann Communication Group, Inc., Know Before You Owe: Evolution of the Integrated TILA-RESPA Disclosures (July 9, 2012), at 254-56 (Round 9, Version 1).
[96] *Id.*
[97] This language was included in the disclosure testing in Round 10.

Finally, comment 35(c)(5)(i)-1 reflects without change a proposed comment clarifying 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. This interpretation is consistent with the statutory language requiring the creditor to provide a disclosure to "the applicant." This interpretation is also consistent with comment 14(a)(2)(i)-1 in Regulation B, which interprets the requirement in § 1002.14(a)(2)(i) that creditors notify applicants of the right to receive copies of appraisals. 12 CFR 1002.14(a)(2) and comment 14(a)(2)(i)-1. This aspect of existing Regulation B is retained in the Bureau's 2013 ECOA Appraisals Final Rule, in § 1002.14(a)(1) and comment 14(a)-1.

35(c)(5)(ii) Timing of Disclosure

TILA section 129H(d) requires that the appraisal notice be provided at the time of the application. 15 U.S.C. 1639h(d). Consistent with this requirement, and recognizing that the "higher-risk" status of the proposed loan would not necessarily be determined at the precise moment of the application, the Agencies proposed to require that the TILA section 129H notice "be mailed or delivered not later than the third business day after the creditor receives the consumer's application." The proposed requirement also stated that, if the notice is not provided to the consumer in person, the consumer is presumed to have received the notice three days after its mailing or delivery.

The final rule adopts this provision with two changes. First, the final rule omits the proposed language providing that "[i]f the disclosure is not provided to the consumer in person, the consumer is presumed to have received the disclosure three business days after they are mailed or delivered." While commenters did not address the issue, the Agencies have concluded that the date of consumer receipt in this context is not relevant. By contrast, as discussed in the section-by-section analysis for § 1026.35(c)(6), below, the Agencies emphasize in the final rule the relevance of the date that a consumer receives the copy of the appraisal. Second, the final rule provides that, in the case of an application for a loan that is not an HPML at the time of application, but whose rate is set at an HPML level after application, the disclosure must be delivered or placed in the mail not later than the third business day after the creditor determines that the loan is an HPML.

Public Comments on the Proposal

In the proposal, the Agencies asked for comment on whether providing the notification at some other time would be more beneficial to consumers, and how the notification should be provided when an application is submitted by telephone, facsimile, or electronically. The Agencies further asked whether, in cases such as in-person or telephone applications, the notice should be provided at the time the application is received, or as part of the application. The Agencies also requested comment on whether a creditor who has a reasonable belief that the transaction will not be a "higher-risk mortgage loan" (now, HPML) at the time of application, but later determines that the applicant only qualifies for an HPML, should be allowed an opportunity to give the notice at some later time in the application process.

Timing issues for the HPML appraisal notice. The majority of commenters – banks, major industry trade associations, and a software and document service provider – supported a timing requirement that would allow them to integrate the HPML appraisal notice into the TILA-RESPA Loan Estimate (as proposed in the 2012 TILA-RESPA Proposal[98]), using the same disclosure timing requirement as proposed for that disclosure – within three business days after the application. This timing requirement is consistent with the Agencies' proposal for the HPML

[98] 77 Fed. Reg. 51116 (Aug. 23, 2012).

disclosure. These commenters offered three reasons why an earlier deadline would be inappropriate:

- The trade associations and the service provider noted that the lender cannot charge an appraisal fee before the TILA Good Faith Estimate (GFE) is disclosed and the consumer elects to proceed. *See* § 1026.19(a)(1)(ii) As a result, there is no value to an appraisal notice that precedes the TILA GFE.
- One of the banks asserted that it would be difficult for a creditor to comply with a deadline for the notice that is any earlier than the TILA GFE disclosure deadline, because the rate and therefore "higher-risk mortgage" status of a loan is not typically known earlier. Similarly, the service provider also added that it would be unrealistic to expect the creditor to determine the status while the applicant is submitting the application.
- The service provider also noted that consumers prefer integrated disclosures.

Two community banks and a State bank trade association submitted substantially identical comments opposing the three-business-day deadline, however. These commenters argued that complying with the notice requirement in the first few days after the application will slow the loan approval process and increase loan costs. These commenters called instead for a 10 business day deadline.

No commenters responded to the question in the proposed rule of whether the notice should be provided at the time the application is received, or as part of the application.

Potential need for a mechanism to provide the notice later. Two banks, a credit union trade association at the State level, and a service provider supported including a method in the rule for a creditor to comply with the disclosure requirement if the loan is determined to be an HPML after the time of application. For example, if the rate were not locked, HPML status could arise later in the application process when the rate is set. One large bank noted, however, that if the language in the notice under this rule is the same as in the ECOA notice, then there would be no need to allow this type of cure right for loans that are subject to ECOA (*i.e.*, first-lien dwelling-secured HPMLs).

Discussion

Again, under § 1026.35(c)(5)(ii) of the final rule, the disclosure required under § 1026.35(c)(5)(i) shall be delivered or placed in the mail no later than the third business day after the creditor receives the consumer's application for a higher-priced mortgage loan subject to § 1026.35(c). In the case of a loan that is not a higher-priced mortgage loan subject to § 1026.35(c) at the time of application, but becomes a higher-priced mortgage loan subject to § 1026.35(c) after application, the disclosure must be delivered or placed in the mail not later than the third business day after the creditor determines that the loan is a higher-priced mortgage loan subject to § 1026.35(c).

Timing issues for the HPML appraisal notice. In § 1026.35(c)(5)(ii), the final rule adopts the proposed timing requirement of three business days after application. Congress did not define the statutory phrase "at the time of the application" when describing when the HRM appraisal notice must be provided. The Agencies believe that the three-business-day timeframe in the proposed rule is a reasonable and appropriate interpretation of the statute. As noted, commenters generally supported a timeframe that would allow for including the notice in the proposed combined TILA-RESPA Loan Estimate, which would be provided within three business days after the application. No commenter suggested that the Agencies should mandate either an earlier or separate notice. Industry commenters correctly pointed out that the appraisal charge cannot be levied prior to the TILA GFE (and, as proposed, the TILA-RESPA Loan

Estimate) being provided in any event. As a result, it appears unlikely that creditors would order appraisals before this time, so consumers would not appear to have a significant need to receive the appraisal notice either earlier or separately from the GFE or Loan Estimate. Adding new separate notices could increase the volume of information consumers receive, and potentially decrease consumer understanding.

The Agencies decline to adopt a timing requirement of more than three business days after application, as some commenters suggested. The statute requires that the disclosure be provided "at application," and a three-business-day timing requirement implementing this would be consistent with the application-related disclosure requirements of other residential mortgage rules, most notably the current GFE and proposed TILA-RESPA Loan Estimate discussed above. *See, e.g.*, § 1026.19(a)(1)(i); 77 FR 51116 (Aug. 23, 2012).

Potential need for a mechanism to provide the notice later. As one commenter noted, clarification may be needed on how a creditor could comply with the notice requirement when the loan becomes an HPML more than three days after application due to the higher-priced rate being set at a later date. As one commenter noted, this clarification would not be necessary for first-lien loans. ECOA, as implemented in Regulation B of the Bureau's 2013 ECOA Appraisals Final Rule, requires notice within three business days after application for all first-lien dwelling-secured loans, regardless of whether they are HPMLs. ECOA section 701(e)(5), 15 U.S.C. 1691(e)(5); 2013 ECOA Appraisals Final Rule § 1002.14(a)(1). Further, the HPML appraisal notice is integrated with the ECOA appraisal notice. *See* 2013 ECOA Appraisals Final Rule, § 1002.14(b) and appendix C, Form C-9. As the final rule makes clear, by complying with the ECOA notice requirement, the creditor would automatically comply with the HPML appraisal notice requirement, even if the creditor had not yet determined that the loan would be an HPML.

Again, § 1026.35(c)(5)(i) provides that "[c]ompliance with the disclosure requirement in Regulation B § 1002.14(a)(2) satisfies the requirements of [the HPML appraisal disclosure requirement of § 1026.35(c)(5)(i)]."

By contrast, the ECOA appraisal notice requirement does not apply to subordinate-lien loans. Thus, for subordinate-lien mortgage creditors, a rate increase that occurs more than three business days after application (*i.e.*, after the required HPML appraisal rule disclosure should have been given) could trigger the HPML notice requirement. Accordingly, the Agencies are adopting additional regulation text providing that a creditor may issue the HPML appraisal notice within three business days of determining the rate.

35(c)(6) Copy of Appraisals

35(c)(6)(i) In General

Consistent with TILA section 129H(c), the proposal required that a creditor must provide a copy of any written appraisal performed in connection with a higher-risk mortgage loan (now HPML) to the applicant. 15 U.S.C. 1639h(c). A proposed comment clarified that when two or more consumers apply for a loan subject to this section, the creditor is required to give the copy of required appraisals to only one of the consumers.

The Agencies received no comments on these aspects of the proposal and, in § 1026.35(c)(6)(i) and comment 35(c)(6)(i)-1, adopt them without change.

35(c)(6)(ii) Timing

TILA section 129H(c) requires that the appraisal copy must be provided to the consumer at least three days prior to the transaction closing date. 15 U.S.C. 1639h(c). The proposal required creditors to provide copies of written appraisals no later than "three business days" prior to consummation of the higher-risk mortgage loan (now HPML). The Agencies did not receive public comment on this aspect of the proposal, but are making certain changes to the proposal, explained below. Specifically, the Agencies have revised the proposed timing requirement to include a timing rule for loans that are not consummated. Thus, under new § 1026.35(c)(6)(ii), creditors must provide a copy of an appraisal required under § 1026.35(c)(6)(i):

- no later than three business days prior to consummation of the higher-priced mortgage loan; or
- in the case of a loan that is not consummated, no later than 30 days after the creditor determines that the loan will not be consummated.

For consistency with the other provisions of Regulation Z, the proposal also used the term “consummation” instead of the statutory term “closing” that is used in TILA section 129H(c). 15 U.S.C. 1639h(c). The term “consummation” is defined in § 1026.2(a)(13) as the time that a consumer becomes contractually obligated on a credit transaction. The Agencies have interpreted the two terms as having the same meaning for the purpose of implementing TILA section 129H. 15 U.S.C. 1639h. The Agencies did not receive comment on this aspect of the proposal, and adopt the proposed term “consummation” in § 1026.35(c)(6)(ii).

As noted, TILA’s requirement for when a creditor must give a copy of the appraisal to the consumer is “at least 3 days prior to the transaction closing date.” TILA section 129H(c), 15 U.S.C. 1639h(c). Thus, the timing requirement is clear for consummated loans.

The Agencies interpret the statute, however, to require that a copy of the appraisal also be given to HPML applicants when their loans do not close because they are denied or withdrawn, or for any other reason. In reaching this interpretation, the Agencies note that TILA section 129H specifies that the appraisal copy shall be provided “to the applicant,” without suggesting that only applicants whose loans are closed are entitled to a copy. In addition, the requirement refers to appraisals that are "conducted," a term whose meaning is independent of whether the loan closes. In the case of applicants' loans that do not close, the Agencies are adopting a requirement that the appraisal be provided "no later than 30 days after the creditor determines that the loan will not be consummated." § 1026.35(c)(6)(ii)(A). The Agencies believe that this timing requirement is a reasonable interpretation of the statute, which is silent on the matter. The timing requirement is clear, which the Agencies believe will reduce compliance burden and risks for creditors, and generally consistent with longstanding timing requirements for providing copies of appraisals under existing Regulation B, 12 CFR 1002.14(a)(2)(ii). The approach is also reflected in the Bureau's 2013 ECOA Appraisals Final Rule in § 1002.14(a)(1).

In addition, as stated in the proposal, the Agencies believe that requiring that the appraisal be provided three "business" days in advance of consummation is a reasonable interpretation of the statute and is consistent with the Agencies' interpretation of the statutory term "days" used in the Bureau's 2013 ECOA Appraisals Final Rule, which implements the appraisal requirements of new ECOA section 701(e)(1). *See* 15 U.S.C. 1691(e)(1). The Agencies did not receive comment on this aspect of the proposal, and adopt the proposed language "no later than three business days prior to consummation" in § 1026.35(c)(6)(ii).

To ensure that the consumer actually receives the appraisal in advance of consummation so that the consumer can use it to inform the consumer's credit decision, comment 35(c)(6)(ii)-1 explains that, for purposes of the requirement to provide a copy of the appraisal three days before consummation, "provide" means "deliver." This comment further explains that delivery occurs three business days after mailing or delivering the copies to the last-known address of the applicant, or when evidence indicates actual receipt by the applicant (which, in the case of electronic receipt must be based upon consent that complies with the Electronic Signatures in

Global and National Commerce Act (E-Sign Act) (15 U.S.C. 7001 *et seq*.)), whichever is earlier. Comment 35(c)(6)(ii)-2 clarifies that, for appraisals prepared by the creditor's internal appraisal staff, the date of "receipt" is the date on which the appraisal is completed.

Finally, comment 35(c)(6)(ii)-3 clarifies that the ECOA provision allowing a consumer to waive the requirement that the appraisal copy be provided three business days before consummation, does not apply to higher-priced mortgage loans subject to § 1026.35(c). ECOA section 701(e)(2), 15 U.S.C. 1691(e)(2), implemented in the 2013 ECOA Appraisals Final Rule, Regulation B § 1002.14(a)(1). The comment further clarifies that a consumer of a higher-priced mortgage loan subject to § 1026.35(c) may not waive the timing requirement to receive a copy of the appraisal under § 1026.35(c)(6)(i).

35(c)(6)(iii) Form of Copy

Section 1026.31(b) currently provides that the disclosures required under subpart E of Regulation Z may be provided to the consumer in electronic form, subject to compliance with the consumer consent and other applicable provisions of the E-Sign Act. In the proposal, the Agencies stated their belief that it is also appropriate to allow creditors to provide applicants with copies of written appraisals in electronic form if the applicant consents to receiving the copies in this form. Accordingly, the proposal provided that any copy of a written appraisal may be provided to the applicant in electronic form, subject to compliance with the consumer consent and other applicable provisions of the E-Sign Act.

Public Comments on the Proposal

Two commenters – a bank holding company and a credit union – requested that the final rule not impose the E-Sign Act requirement of consumer consent to receiving HPML appraisals electronically. The first commenter indicated that challenges with the E-Sign Act compliance may result in issuing a duplicate copy in paper form. The second commenter indicated that these challenges may lead institutions to refuse to provide appraisal copies electronically (to the detriment of those consumers who prefer to receive them this way). A third commenter – a credit union trade association – supported the option of electronic delivery, but did not challenge the proposed E-Sign consent requirement.

Discussion

The E-Sign Act generally requires that, before written consumer disclosures are made electronically, the consumer receive certain prescribed notices and consent to the electronic disclosures in a manner that reasonably demonstrates the ability to access the information that will be disclosed electronically. The E-Sign Act generally applies to statutes that require consumer disclosures "in writing." 15 U.S.C. § 7001(c)(1). It is unclear from the comments whether this E-Sign consent requirement would place a significant burden on creditors. The Agencies continue to believe that the proposed clarification that the E-Sign Act applies to providing copies of the appraisal is appropriate and notes that it is consistent with the Bureau's approach in the 2013 ECOA Appraisals Final Rule. Thus, in § 1026.35(c)(6)(iii), this clarification is adopted as proposed.

35(c)(6)(iv) No Charge for Copy of Appraisal

TILA section 129H(c) provides that a creditor shall provide one copy of each appraisal conducted in accordance with this section in connection with a higher-risk mortgage to the applicant without charge. 15 U.S.C. 1639h(c). In the proposal, the Agencies interpreted this provision to prohibit creditors from charging consumers for providing a copy of written appraisals required for higher-risk mortgage loans. Accordingly, the proposal provided that a creditor must not charge the consumer for a copy of a written appraisal required to be provided to the consumer pursuant to new § 1026.35(c)(6)(i).

A proposed comment clarified that the creditor is prohibited from charging the consumer for any copy of a required appraisal, including 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.

The Agencies received no comments on this aspect of the proposal and adopt the proposed regulation text and comment without change in § 1026.35(c)(6)(iv) and comment 35(c)(6)(iv)-1.

35(c)(7) Relation to Other Rules

Section 1026.35(c)(7) clarifies that the final rule was adopted jointly by the Agencies. This provision states that the Board is codifying the HPML appraisal rules at 12 CFR 226.43 *et seq.*; the Bureau is codifying the HPML appraisal rules at 12 CFR 1026.35(a) and (c); and the OCC is codifying the HPML appraisal rules at 12 CFR Part 34 and 12 CFR Part 164. Section 1026.35(c)(7) further clarifies that there is no substantive difference among the three sets of rules.

The NCUA and FHFA are adopting the rules as published in the Bureau's Regulation Z at 12 CFR 1026.35(a) and (c), by cross-referencing these rules in 12 CFR 722.3 and 12 CFR Part 1222, respectively. The FDIC is adopting the Bureau's Regulation Z at 12 CFR 1026.35(a) and (c) without a cross-reference.

As noted above at the beginning of the section-by-section analysis, § 1026.35(a) is re-published in the final rule for ease of reference, and the joint rulemaking authority extends to § 1026.35(c).

V. Bureau's Section 1022(b)(2) of the Dodd-Frank Act

Overview

In developing the final rule, the Bureau has considered potential benefits, costs, and impacts to consumers and covered persons.[99] The Bureau is issuing this final rule jointly with the Federal financial institutions regulatory agencies and FHFA, and has consulted with these agencies, HUD, and the FTC, including regarding consistency with any prudential, market, or systemic objectives administered by such agencies. The Bureau also has considered the comments filed by industry, consumer groups, and others as described in the section-by-section analysis. Data received from commenters relating to potential benefits and costs, such as the cost of an appraisal, is discussed below.

As discussed above, the final rule implements section 1471 of the Dodd-Frank Act, which establishes appraisal requirements for certain HPMLs. Consistent with the statute, the final rule allows a creditor to originate a covered HPML transaction only if the following conditions are met:

- The creditor obtains a written appraisal;
- The appraisal is performed by a certified or licensed appraiser; and
- The appraiser conducts a physical property visit of the interior of the property.

[99] Specifically, Section 1022(b)(2)(A) 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 Act; and the impact on consumers in rural areas.

In addition, as required by the Act, the final rule requires a creditor in a covered HPML transaction to obtain an additional written appraisal, at no cost to the borrower, if the transaction has each of the following characteristics (subject to certain exemptions, as discussed below):

- The HPML will finance the acquisition of the consumer's principal dwelling;
- The seller acquired the property within 180 days prior to the consumer's purchase agreement (measured from the date of the consumer's purchase agreement); and
- The consumer is acquiring the home for a price that exceeds the price at which the seller acquired the home by more than 10 percent (if the seller acquisition was within 90 days of the consumer's purchase agreement) or by more than 20 percent (if the seller acquisition was within the past 91 to 180 days of the consumer's purchase agreement).

The additional written appraisal, from a different licensed or certified appraiser, generally must include the following information: an analysis of the difference in sale prices (*i.e.*, the price at which the seller acquired the property and the price at which the consumer would acquire the property as set forth in the consumer's purchase agreement), changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale.

The final rule also requires that within three days of the application, the creditor provide the applicant with a brief disclosure statement that the creditor may charge the applicant for an appraisal, that the creditor will provide the applicant a copy of any appraisal, and that the applicant may choose to have a separate appraisal conducted at the expense of the applicant. Finally, the final rule requires that the creditor provide the consumer with a free copy of any written appraisals obtained for the transaction at least three (3) business days before consummation, or within 30 days of determining the transaction will not be consummated.

In many respects, the final rule codifies mortgage lenders' current practices. In outreach calls to industry, all respondents reported requiring the use of full-interior appraisals in 95 percent or more of first-lien transactions[100] and providing copies of appraisals to borrowers as a matter of course if such a loan is originated.[101] The convention of using full-interior appraisals on first liens has been developing to improve underwriting quality, and the implementation of this rule would assure that the practice would continue even under different market conditions.

The Bureau notes that many of the provisions in the final rule implement self-effectuating amendments to TILA. The costs and benefits of these provisions arise largely or in some cases entirely from the statute and not from the rule that implements them. This rule provides benefits compared to allowing these TILA amendments to take effect without implementing regulations, however, by clarifying parts of the statute that are ambiguous. Greater clarity on these issues covered by the rule should reduce the compliance burdens on covered persons by reducing costs for attorneys and compliance officers as well as potential costs of over-compliance and unnecessary litigation.[102]

Section 1022 permits the Bureau to consider the benefits, costs, and impacts of the final rule solely compared to the state of the world in which the statute takes effect without an implementing regulation. To provide the public better information about the benefits and costs of the statute, however, the Bureau has chosen to consider the benefits, costs, and impacts of the

[100] Respondents include a large bank, a trade group of smaller depository institutions, a credit union, and an independent mortgage bank.
[101] Respondents include a large bank, a trade group of smaller depository institutions, and an independent mortgage bank.
[102] While it is possible that some clarifications would put greater burdens on creditors as compared to what the statute would ultimately be found to mandate, the Bureau believes that the rule's clarifying provisions generally mitigate burden.

major provisions of the final rule against a pre-statutory baseline (*i.e.*, the benefits, costs, and impacts of the relevant provisions of the Dodd-Frank Act and the regulation combined).[103]

The Bureau has relied on a variety of data sources to analyze the potential benefits, costs, and impacts of the final rule.[104] However, in some instances, the requisite data are not available or are quite limited. Data with which to quantify the benefits of the rule are particularly limited. As a result, portions of this analysis rely in part on general economic principles to provide a qualitative discussion of the benefits, costs, and impacts of the rule.

The primary source of data used in this analysis is data collected under the Home Mortgage Disclosure Act (HMDA).[105] Because the latest wave of complete data available is for

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[103] The Bureau has discretion in any rulemaking to choose an appropriate scope of analysis with respect to potential benefits and costs and an appropriate baseline. The Bureau, as a matter of discretion, has chosen to describe a broader range of potential effects to more fully inform the rulemaking.

[104] The estimates in this analysis are based upon data and statistical analyses performed by the Bureau. To estimate counts and properties of mortgages for entities that do not report under the Home Mortgage Disclosure Act (HMDA), the Bureau has matched HMDA data to Call Report data and National Mortgage Licensing System (NMLS) and has statistically projected estimated loan counts for those depository institutions that do not report these data either under HMDA or on the NCUA call report. The Bureau has projected originations of higher-priced mortgage loans for depositories that do not report HMDA in a similar fashion. These projections use Poisson regressions that estimate loan volumes as a function of an institution's total assets, employment, mortgage holdings, and geographic presence. Neither HMDA nor the Call Report data have loan level estimates of debt-to-income (DTI) ratios that, in some cases, determine whether a loan is a qualified mortgage. To estimate these figures, the Bureau has matched the HMDA data to data on the historic-loan-performance (HLP) dataset provided by the FHFA. This allows estimation of coefficients in a probit model to predict DTI using loan amount, income, and other variables. This model is then used to estimate DTI for loans in HMDA.

[105] HMDA, enacted by Congress in 1975, as implemented by the Bureau's Regulation C requires lending institutions annually to report public loan-level data regarding mortgage originations. For more information, see http://www.ffiec.gov/hmda. It should be noted that not all mortgage lenders report HMDA data. The HMDA data capture roughly 90–95 percent of lending by the FHA and 75–85 percent of other first-lien home loans, in both cases including first liens on manufactured homes (which in some cases are subject to the final rule). HUD, Office of Policy Development and Research (2011), "A Look at the FHA's Evolving Market Shares by Race and Ethnicity," *U.S. Housing Market Conditions* (May), pp. 6–12. Depository institutions (including credit unions) with assets less than $40 million (in 2011), for example, and those with branches exclusively in non-metropolitan areas and those that make no home purchase loan or loan refinancing a home purchase loan secured by a first lien on a dwelling, are not required to report under HMDA. Reporting requirements for non-depository institutions depend on several factors, including whether the company made fewer than 100 home purchase loans or refinancings of home purchase loans, the dollar volume of mortgage lending as share of total lending, and whether the institution had at least five applications, originations, or purchased loans from metropolitan areas. Robert B. Avery, Neil Bhutta, Kenneth P. Brevoort & Glenn B. Canner, *The Mortgage Market in 2011: Highlights from the Data Reported under the Home Mortgage Disclosure Act*, 98 Fed. Res. Bull., December 2012, n.6. In addition, HMDA data used in this analysis does not include transactions secured by properties located in U.S. territories, or refinance transactions where the existing loan is already a refinance or a subordinate lien. Although the TILA HRM rule would apply to otherwise

loans made in calendar year 2011, the empirical analysis generally uses the 2011 market as the baseline. Data from the 4th quarter 2011 bank and thrift Call Reports,[106] the 4th quarter 2011 credit union call reports from the NCUA, and de-identified data from the National Mortgage Licensing System (NMLS) Mortgage Call Reports (MCR)[107] for the 4th quarter of 2011 also were used to identify financial institutions and their characteristics. Most of the analysis relies on a dataset that merges this depository institution financial data from Call Reports with the data from HMDA including HPML counts that are created from the loan-level HMDA dataset. The unit of observation in this analysis is the entity: if there are multiple subsidiaries of a parent company, then their originations are summed and revenues are total revenues for all subsidiaries.

Other portions of the analysis rely on property-level data regarding parcels and their related financing from DataQuick[108] and on data on the location of certified appraisers from the Appraisal Subcommittee Registry.[109] Tabulations of the DataQuick data are used for estimation

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covered HPMLs in these categories, the Bureau does not believe there are a high number of transactions in these categories. To the extent this gap understates costs, that effect will be at least partially offset by the overstatement resulting from including other data on transactions that are not subject to the rule.

[106] Every national bank, State member bank, and insured nonmember bank is required by its primary Federal regulator to file consolidated Reports of Condition and Income, also known as Call Report data, for each quarter as of the close of business on the last day of each calendar quarter (the report date). The specific reporting requirements depend upon the size of the bank and whether it has any foreign offices. For more information, see http://www2.fdic.gov/call_tfr_rpts/.

[107] The NMLS is a national registry of non-depository financial institutions including mortgage loan originators. Portions of the registration information are public. The Mortgage Call Report data are reported at the institution level and include information on the number and dollar amount of loans originated, and the number and dollar amount of loans brokered. The Bureau noted in its Summer 2012 mortgage proposals that it sought to obtain additional data to supplement its consideration of the rulemakings, including additional data from the NMLS and the NMLS Mortgage Call Report, loan file extracts from various lenders, and data from the pilot phases of the National Mortgage Database. Each of these data sources was not necessarily relevant to each of the rulemakings. The Bureau used the additional data from NMLS and NMLS Mortgage Call Report data to better corroborate its estimate the contours of the non-depository segment of the mortgage market. The Bureau has received loan file extracts from three lenders, but at this point, the data from one lender is not usable and the data from the other two is not sufficiently standardized nor representative to inform consideration of the final rule. Additionally, the Bureau has thus far not yet received data from the National Mortgage Database pilot phases. The Bureau also requested that commenters submit relevant data. All probative data submitted by commenters are discussed in this final rule.

[108] DataQuick is a database of property characteristics on more than 120 million properties and 250 million property transactions.

[109] The National Registry is a database containing selected information about State certified and licensed real estate appraisers and is publicly available at https://www.asc.gov/National-Registry/NationalRegistry.aspx.

of the frequency of properties being sold within 180 days of a previous sale. The Appraisal Subcommittee's Registry is used to describe the availability of appraisers.

Potential Benefits of the Rule for Covered Persons and Consumers

In a mortgage transaction, the appraisal helps the creditor avoid lending based on an inflated valuation of the property, and similarly helps consumers avoid borrowing based upon an inflated valuation. Assuming that full-interior appraisals conducted by a certified or licensed appraiser are more accurate than other valuation methods, the rule would improve the quality of home valuations for those transactions where such an appraisal would not be performed currently. While the appraisal is used by the creditor, the improved valuation also can prevent inflated valuations that would lead consumers to borrowing that would not be supported by their true home value, as well as deflated valuations (such as those that do not value an interior which is of different than average quality) that can lead consumers to be eligible for a narrower class of loan products that are priced less advantageously. The requirement that a second appraisal be conducted in certain circumstances would further reduce the likelihood of an inflated sales price for those transactions.

Benefits to covered persons. Transactions where the collateral is overvalued expose the creditor to higher default risk. By tightening valuation standards for a class of transactions that are already priced as higher-risk transactions, the rule may reduce both the risk of default for creditors, as well as more accurately value the collateral available to the creditor in the event of default. Furthermore, by requiring the use of full interior appraisals in transactions involving covered HPMLs, the statute prevents creditors from attempting to compete on price by using less costly and possibly less accurate valuation methods in underwriting. Eliminating the ability to use lower-cost valuation methods, and thereby eliminating price competition on this component of the transaction, may benefit firms that prefer to employ more thorough valuation methods.

Benefits to consumers. The final rule ensures that covered HPML transactions will have a written interior appraisal, and in some cases a second written interior appraisal, and that consumers will receive an appraisal notice and a copy of these appraisals. These requirements will mostly benefit consumers whose transactions would not already have written interior appraisals a copy of which they receive. The benefits enjoyed by these consumers are described below.

Individual consumers engage in real estate transactions infrequently, so developing the expertise to value real estate is costly and consumers often rely on experts, such as real estate agents, as well as on list prices, to make price determinations. These methods may not lead a consumer to an accurate valuation of a property they intend to purchase. For example, there is evidence that real estate agents sell their own homes for significantly more than other similar homes, which suggests that consumers may not be able to accurately price the homes that they are selling.[110] Other research, this time in a laboratory setting, provides evidence that individuals are sensitive to anchor values when estimating home prices.[111] In such cases, an independent signal of the value of the home should benefit the consumer. Having a professional valuation as a point of reference may help consumers who are applying for a HPML to gain a more accurate

[110] Levitt, Steven and Chad Syverson. "Market Distortions When Agents are Better Informed: The Value of Information In Real Estate Transactions." The Review of Economics and Statistics 90 no.4 (2008): 599-611.
[111] Scott, Peter and Colin Lizieri. "Consumer House Price Judgments: New Evidence of Anchoring and Arbitrary Coherence." Journal of Property Research 29 no. 1 (2012): 49-68.

understanding of the home's value and improve overall market efficiency, relative to the case where the knowledge of true valuations is more limited.[112]

While the consumer can order an appraisal voluntarily at any time, an especially valuable time for the consumer to receive a copy of an appraisal is before closing an HPML – whether it is for a home purchase, a refinance, or a home improvement. Undoubtedly, some consumers are aware of the benefits of an appraisal, and could have decided for themselves whether they want to pay for it if one was not required or otherwise prepared and provided under standard industry practice. However, other consumers may be unaware of the benefits of an appraisal in terms of improving accuracy of a home valuation, and to these consumers the rule is especially valuable in an HPML transaction that would not otherwise include an appraisal. Moreover, even the consumers who are aware of the benefits would not be able to use the self-ordered appraisal for any transactions with creditors, since those require creditor-ordered valuations.

The Bureau believes that ensuring HPML borrowers receive appraisals ensures that they will have more accurate information about the value of their dwelling, and therefore about their net worth and whether they have any equity in their dwelling. For transactions that would already include the appraisal, the rule ensures that in similar transactions consumers will continue to have an appraisal; for other transactions, the rule will result in the appraisal. In either case, more accurate information leads to better decisions and can lead to more investment in the property in some cases by removing the uncertainty over the value of the dwelling. The appraisal may also help to inform the consumer of whether they may be overpaying for the

[112] For example, in Quan and Quigley's theoretical model where buyers and sellers have incomplete information, trades are decentralized, and prices are the result of pairwise bargaining, "[t]he role of the appraiser is to provide information so that the variance of the price distribution is reduced." Quan, Daniel and John Quigley. "Price Formation and the Appraisal Function in Real Estate Markets." Journal of Real Estate Finance and Economics 4 (1991): 127-146.

property with a new home purchase, about to invest more into a property that might be valued at less than they think with a home improvement loan, or about to pay the refinance cost on a property that they should sell instead. The latter two points are especially valuable for consumers who are in negative equity, or "underwater" situations (where the loan amount exceeds the value of the dwelling). A consumer who finds out that she is not underwater, when she thought that she might have been, has an incentive to continue investing in the property and make sure that she does not lose it in foreclosure or otherwise default. Conversely, a consumer who finds out that he is underwater, when he thought that he might not have been, might have second thoughts about any investments, and will potentially want to pursue loss mitigation options or, if they do not succeed and the consumer is facing financial difficulties or default, agree on a short-sale or on a deed-in-lieu of foreclosure with the creditor.

Aside from the aforementioned decisions, depending on the alternative valuation, an appraisal can help the consumer to lower their property tax, to forgo private mortgage insurance (PMI), and to choose the correct property value for insurance purposes. A lower loan-to-value (LTV) ratio might also result in a lower interest rate on the loan, all else equal, as discussed further below. Again, the final rule ensures these benefits are available to consumers in transactions that do not currently have appraisals or provide copies to applicants.

If a borrower is prepared to pay an inflated price for a property, then an appraisal that reflects its value more accurately may prevent the transaction from being completed at the inflated price and consequently, at a higher loan amount, which would be more costly to the consumer who, in the case of an HPML borrower, also may have fewer resources to repay the loan. This is particularly true when considering that transactions subject to the rule will be those HPMLs that are not qualified mortgages, and which therefore may involve higher points, greater fees, or a higher debt-to-income ratio, among other differences. In addition to the direct costs of paying more than the true value for a property, buying an overvalued property is associated with higher risk of default. If a property that is sold shortly after its previous sale is more likely to have an inflated price, since it may have been purchased the first time with the intention to improve the property quickly and resell it for a profit, the additional appraisal requirement also would help ensure an accurate estimate of the value of the property. This would be particularly true in transactions involving fraudulent flipping using an inadequate or improperly performed first appraisal.[113] Ensuring a more accurate valuation of a flipped property might be especially valuable to a consumer when borrowing an HPML (due to its higher price). In the case of subordinate-lien transactions, the full-interior appraisal requirement may prevent borrowers on HPMLs from extracting too much equity if their property is overvalued by other valuation methods. Accordingly, the appraisals required by the final rule could reduce the chance consumers would be in a negative equity or near negative equity situation, which can limit refinancing and selling opportunities.

At the same time, if a borrower is prepared to take out an HPML based upon the creditor's use of a valuation other than an interior appraisal, that valuation may be less likely to take into account unique characteristics of the subject property, such as its setting in the immediate neighborhood, its views, the quality of the exterior or the residential structure, or its interior condition. For borrowers where direct assessments of those characteristics would have improved the valuation, the price of the loan may be based upon an LTV ratio that is overstated, and the loan may be overpriced to the extent that higher LTVs correlate with higher-priced loans.

[113] Congress has noted a concern, for example, that parties to a flipping transaction "can often find an appraiser to inflate the home's value." H.Rep. 111-94 (May 4, 2009) at 59.

The final rule also may support greater consumer choice in HPML transactions, to the extent new creditors treat the appraisals required as portable. For example, the FHA has taken steps to ensure appraisal portability in the situation of an "applicant who has gotten to the appraisal stage of the home loan process, but" the applicant decides he or she is "dissatisfied with [the] lender and decide[s] to find a new one."[114] The final rule ensures that if consumers would not otherwise have an appraisal in HPML transactions for which they have applied, then they will have an appraisal that may be able to be used in alternative transactions that the consumer may pursue.

Codifying HPML valuation standards across the industry likely would simplify the shopping process for consumers who receive HPML offers. First, for consumers in HPML transactions that would not have otherwise included an appraisal, the appraisals required by the rule may help to improve consumers' understanding of the determinants of the value of the property that they intend to purchase. In cases where a loan is denied due to an appraiser valuing the property at less than the contract price, the appraisal will include support for its findings of the lower value, which may help the consumer in future negotiations or property searches. Second, codifying appraisal standards across the industry would simplify the shopping process for consumers by making the process of applying for HPMLs more consistent between lenders. Full-interior appraisals typically cost more than other valuation methods, and appraisal costs are often passed on to consumers. Consumers may not understand the differences between different valuation methods or know that different creditors will use different methods, and therefore may benefit from the standardization the rule can be expected to promote.

[114] *See* FHA FAQ "Are FHA Home Loan Appraisals Portable?" available at http://www.fha.com/fha_article.cfm?id=350, citing FHA Mortgagee Letter 09-29 (Sept. 18, 2009) (stating that FHA programs allow for appraisal portability).

The final rule also will ensure that borrowers in covered HPML transactions involving subordinate liens receive a notice informing them about the appraisal process, of their ability to order their own appraisal, and that they will receive copies of any appraisals at least three business days prior to the consummation. Under ECOA section 701(e) and its implementing rules, applicants in transactions secured by a first lien on a dwelling will receive this notice and a copy of an appraisal; under this provision in the statute and the Bureau’s 2013 ECOA Appraisals Final Rule, which takes effect on January 18, 2014, these requirements do not apply to subordinate lien transactions, however. The final rule fills this gap for borrowers on covered HPMLs, ensuring they are better informed prior to entering into subordinate lien loans, such as for home improvement purposes and other common purposes.

Potential Costs of the Rule for Covered Persons

The costs of the rule, which are predominantly related to compliance, are more readily quantifiable than the benefits and can be calculated based on the mix of loans originated by an entity and the number of employees at that entity. These compliance costs may be considered as the discrete tasks that would be required by the rule. These can be separated into costs that are associated with the origination of a single HPML and the costs of reviewing and implementing the regulation.

Costs per HPML. The costs of the rule for covered persons that derive from requirements to obtain appraisals depend on the number of appraisals that would be conducted, above and beyond current practice, and the degree to which those costs are passed to consumers. For HMDA reporters, counts of HPMLs that are purchase-money loans, first-lien refinance loans, or closed-end subordinate lien loans are computed from the loan-level HMDA data. Accepted statistical methods are used to project loan counts for non-HMDA reporting depository institutions.[115] Estimates of the number of loan officers are calculated from similar projections of applications per institution.

The calculation of costs for IMBs uses a slightly different approach.[116] Consistent with the results from HMDA-reporting IMBs, the Bureau estimates the costs to IMBs by multiplying a cost per loan by the total number of loans originated by IMBs. To obtain a count of full-time equivalent employees, this number is imputed for HMDA-reporting IMBs based on the number of applications (assuming 1.38 days per loan application).[117]

Based on these data sources, the Bureau estimates that there were approximately 292,000 HPMLs in 2011. Of these, the Bureau estimates that 146,000 were purchase-money mortgages, 116,000 were first-lien refinancings, and 30,000 were closed-end subordinate lien mortgages that were not part of a purchase transaction.[118] Due to the exemptions from the rule, only a subset of HPMLs will be covered by the rule. Qualified mortgages, for example, are exempt from the final rule, as are reverse mortgages, loans for initial construction, temporary bridge loans, and new manufactured housing sales.[119] Conservatively, the Bureau is preparing this estimate based upon a loan count without subtracting construction loans, temporary bridge loans, loans for new manufactured housing, or reverse mortgages. While these loans are exempt from the final rule, the data sources do not separately break them out and nationally-representative data on the

[115] Poisson regressions are run, projecting loan volumes in these categories on the natural log of characteristics available in the Call Reports (total 1-4 family residential loan volume outstanding, full-time equivalent employees, and assets), separately for each category of depository institutions.
[116] “Independent Mortgage Bank” refers to non-depository mortgage lenders.
[117] Sumit Agarwal and Faye Wang, *Perverse Incentives at the Banks? Evidence from Loan Officers* (Federal Reserve Bank of Chicago Working Paper 2009-08).
[118] Purchase-money mortgages include subordinate-lien HPMLs that were part of a purchase transaction. The Bureau assumes that these loans were part of a transaction where the first-lien mortgage was not a HPML; to the extent that any of these subordinate-lien purchase-money HPMLs were part of a transaction where the first lien mortgage was a HPML the costs imposed by the rule would be double-counted. First-lien refinancings include loans classified as first-lien “home improvement” loans in HMDA.
[119] Very conservatively, the PRA burden estimates for Agencies other than the Bureau do not estimate and exclude the number of HPMLs that are qualified mortgages. By contrast, based upon data available to it, the Bureau does so in this section 1022 analysis and its Regulatory Flexibility Act certification.

number of loans that fall into these specific categories and also meet the HPML definition is not available.[120] Subtracting only those HPMLs that would be qualified mortgages under Regulation Z § 1043(e)[121] results in a loan count of approximately 26,000 HPMLs that are not qualified mortgages, 12,000 of which were purchase-money mortgages, 12,000 of which were first-lien refinancings, and 2,000 of which were closed-end subordinate lien mortgages that were not part of a purchase transaction. These are the number of loans originated annually that the Bureau conservatively estimates currently would be subject to the final rule.

The Bureau estimates that the probability that full-interior appraisals are conducted as part of current practice is 95 percent for purchase-money transactions, 90 percent for refinance transactions, and 5 percent for subordinate lien mortgage transactions.[122] The Bureau therefore estimates that the proposal would lead to full-interior appraisals for approximately 3,800 HPML originations annually that would not otherwise have a full-interior appraisal.[123] A portion of these HPMLs also would be subject to the requirement that lenders obtain a second full-interior appraisal in situations where the home that would secure the higher-risk mortgage is being resold at or within 180 days at a higher price that exceeds the seller's acquisition price by 10 percent (if the seller acquired the property within 90 days) or 20 percent (if the seller acquired the property

[120] Similarly, no subtractions are made for boats, trailers, or mobile homes, which also are exempt from the final rule. The Bureau also notes that HMDA data includes same-creditor refinances with lower rates and new payment schedules, within the meaning of 12 CFR 1026.20(a)(2). For purposes of this analysis, the Bureau assumes the final rule applies to those transactions, which the HMDA data also does not segregate. This assumption also accounts for the fact that these transactions would not be qualified mortgages, under Regulation Z comment 43(a)-1 adopted in the 2013 ATR Final Rule.

[121] The final rule exempts all loans that would meet one or more of the definitions of qualified mortgage in § 1043(e). *See also* 2013 ATR Final Rule, available at http://consumerfinance.gov. These loans are therefore excluded from the HPML count.

[122] As other Agencies noted in the proposed rule, federal regulations do not require interior appraisals in some cases, such as for transactions below $250,000. To the extent creditors in those transactions elect not to order interior appraisals, those transactions would fall within the 5 percent of purchase-money transactions, 10 percent of refinance transactions, and 95 percent of subordinate lien transactions in which the Bureau assumes no interior appraisal is currently performed.

[123] (5%*12,249) + (10%*11,950)+(95%*2,091) = 3,794.

within 91 to 180 days). Based on FHFA estimates from DataQuick noted in the proposal, the Bureau estimates that the proportion of sales that are resales within 180 days is 5 percent. A significant number of HPMLs financing resales would not be subject to the second appraisal requirement, however, due to the price increase thresholds discussed above and to various exemptions from the second appraisal requirement. For purposes of estimating the number of HPMLs that are subject to the second appraisal requirement, however, the Bureau conservatively only excludes the estimated number of loans subject to the exemption for rural loans.[124] The rural exemption excludes 20.6 percent of the relevant market by transaction volume, according to the 2011 HMDA data. The Bureau therefore estimates that this provision of the rule would apply to approximately 500 HPMLs annually.[125] Accordingly, the Bureau estimates that the number of HPMLs subject to only one new interior appraisal under the rule would be 3,800, and the number of HPMLs subject to a second interior appraisal under the rule would be 500, resulting in a combined addition of 4,300 interior appraisals to HPML transactions each year. This combined addition is the estimated total effect of the rule on the number of appraisals each year.[126]

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[124] The Bureau has not been able to locate nationally-representative data on the number of HPMLs that are flips that fall within other categories of transactions that are exempt from the second appraisal requirement.

[125] (12,249 * 5%*(100%-20.6%)) = 486.

[126] The Bureau believes that under the 2013 ATR Final Rule creditors generally will be able to determine at the outset of the application process whether the loan will be a qualified mortgage. Some creditors may, for their own risk management and at their option, over-comply during the application process to mitigate any risk that due to an error the loan as closed or handled post-closing ultimately would not be a qualified mortgage. For example, under the temporary qualified mortgage provision related to GSEs, a creditor may determine early in the application process that a proposed HPML would be a qualified mortgage because it meets the criteria for purchase or guarantee by a GSE consistent with comment 43(e)(4)(iii)-4 in the Bureau's 2013 ATR Final Rule, but later find that the loan is rejected by the GSE as ineligible for reasons unrelated to the HPML rule. For the loan to be a qualified mortgage, it is not necessary that the loan ultimately be purchased or guaranteed by the GSE. But if the original eligibility determination were invalid, then this could create a risk that the loan would not meet the definition of a qualified mortgage. Such a loan potentially still could meet the definition of qualified mortgage on other bases than being eligible for purchase or guarantee by a GSE. But if not, then under this final rule, origination of such a loan would have been a violation if the creditor did not comply with the requirements for HPML appraisals and no other exemption applied. While these situations may be infrequent, some creditors may seek to over-comply in order to

The following discussion considers estimated compliance costs in the order in which they arise in the mortgage origination process. First, the rule requires that the creditor furnish the applicant with the disclosure required by §1026.35(c)(5)(i).[127] The cost of this disclosure – at most, delivery of a single piece of paper with a standardized disclosure that could be delivered with other documents or disclosures – would be very low.[128]

Second, the rule requires the creditor to verify whether a loan is a HPML. However, the Bureau believes this activity does not to introduce any significant costs beyond the regular cost of business because creditors already must compare APRs to APOR for a variety of compliance purposes under existing Regulation Z[129] or to determine if a loan is subject to the protections of the Home Ownership and Equity Protection Act of 1994 (HOEPA).[130]

The third step is an optional one. If a creditor decides to seek to be eligible for the safe harbor provided for in § 1026.35(c)(3)(ii), the creditor likely would take certain steps in the process of ordering and reviewing a full-interior appraisal as prescribed by the rule. The review process is described in the Appendix N of the rule, and the Bureau assumes it will be performed by a loan officer and to take 15 minutes on average (including the very brief time needed to send

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mitigate the risk they may pose. The Bureau does not believe over-compliance, to control for the risk of an erroneous determination by the creditor that the loan was a qualified mortgage, would lead to creditors ordering a significant number of new appraisals above those estimated here.

[127] Creditors must disclose the following statement, in writing, to a consumer who applies for a higher-risk mortgage loan: "We may order an appraisal to determine the property's value and charge you for this appraisal. We will give you a copy of any appraisal, even if your loan does not close. You can also pay for an additional appraisal for your own use at your own cost."

[128] The Bureau notes that creditors in first lien transactions making a disclosure required by Bureau rules implementing ECOA section 701(e) also would automatically satisfy the disclosure requirement under this rule; the final rule. In addition, the disclosure is included in the proposed Loan Estimate as part of the 2012 TILA-RESPA Proposal (*see* 2012 TILA-RESPA Proposal, (published July 9, 2012), *available at* http://files.consumerfinance.gov/f/201207_cfpb_proposed-rule_integrated-mortgage-disclosures.pdf.); if that proposal were adopted, the cost of providing the disclosure would be part of the overall costs of implementing that disclosure.

[129] 12 CFR 1026.35.

[130] 15 U.S.C. § 1639.

a copy to the applicant, as discussed below).[131] Assuming an average total hourly labor cost of loan officers of $48.29, the cost of review per additional appraisal is $12.07.[132] With an estimated total number of annual additional appraisals – pursuant to both the first and second appraisal requirements –of 4,300, the total cost of reviewing those appraisals is $58,000 (rounded to the nearest thousand).[133]

In purchase transactions financed by a covered HPML, creditors also will need to determine whether a second appraisal would be required based upon prior sales or acquisitions involving the property that would secure the loan. This would require labor costs to determine, through reasonable diligence, whether the seller acquired the property in the past 180 days, and if so, at a price that is sufficiently lower than the contract sale price for the current transaction to trigger the second appraisal requirement. The rule provides that reasonable diligence can be performed through reliance on written source documents, which may include, among others, the 10 types of documents listed in new Appendix O to Part 1026. The Bureau believes creditors typically already obtain many of the common source documents for other purposes during the application process for a purchase-money HPML. The Bureau estimates that reasonable diligence would take, on average, 15 minutes of staff time. Because an estimated 95 percent of covered HPML transactions are not flips at all, in many cases this may be determined from the available documentation more quickly than 15 minutes, simply by determining that the seller's

[131] One community bank commenter stated that this estimate was too low, but did not explain the amount of time it believed would be required to review the appraisal under the rule. In any event, the 15 minute assumption is on average. Some appraisals would be assumed to take more time, and others less. To the extent an appraisal is deficient, and is sent for revision and then further review by the creditor upon revision, this is not assumed to be a cost imposed by the rule and rather is part of a standard underwriting process.

[132] (.25 * $48.29) = $12.07. The hourly wage rate is based on the higher of the loan officer wages at depository institutions of $31.69 and at non-depository institution of $32.16. Wages comprised 66.6 percent of compensation for employees in credit intermediation and related fields in Q4 2011, according to the Bureau of Labor Statistics Series ID CMU2025220000000D,CMU2025220000000P, available at http://www.bls.gov/ncs/ect/#tables. All the hourly wage rates below are computed similarly from the same source.

[133] ($12.07 * 4,280) = $58,000 (rounded to the nearest thousand).

acquisition occurred more than 180 days before the borrower's purchase agreement. Of the 5 percent that are flips, creditors may take more time to analyze price differences versus the thresholds in the rule. Thus the 15 minute estimation is an average. The dollar cost per covered HPML loan is therefore $12.07.[134] With total annual non-QM HPMLs that are purchase transactions of 12,000, the total cost per year is estimated to be $148,000 (rounded to the nearest thousand).[135]

The Bureau believes based on outreach that the direct costs of conducting appraisals would be passed through to consumers, except in the case of an additional appraisal that would be required by § 1026.35(c)(4)(i) (requiring an additional appraisal for properties that are the subject of certain 180-day resales).[136] Based on a nationally-representative dataset of the cost of appraisals, which as a standard matter include interior inspections per the URAR form discussed in the section-by-section analysis in this final rule, the Bureau believes that the average cost of each full-interior appraisal is $350.[137] As noted above, the Bureau estimates that 486 second full-interior appraisals would be required each year under the rule, for a total cost to creditors of $170,000 (rounded to the nearest thousand).[138]

Finally, the rule also requires that free copies of appraisals be provided to borrowers at least three business days before the loan is consummated (or within 30 days of determining the

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[134] (.25 * $45.80) = $11.45.

[135] ($12.07 *12,249) = $148,000 (rounded to the nearest thousand).

[136] The final rule, in § 1026.35(c)(4)(v), prohibits the creditor from charging the consumer for the cost of the additional appraisal. For purposes of estimating the cost the rule imposes on creditors, the Bureau assumes that the creditors will not pass through any of the cost of the second appraisal to the consumers.

[137] Based upon the industry dataset used in the proposal, the Bureau calculates the median for the United States overall is $350, the average is $351, and standard deviation is $92. The $350 estimated cost also falls within the range of $225 to $750 cited by industry comments, most of which referred to costs between $300 and $600. While the proposal had assumed a $600 cost, that cost was at the highest state median (Alaska) in the industry dataset. Upon further review, the Bureau believes that $350 is a more accurate estimate of the average cost and that using a $600 cost would, while being conservative, also overestimate the cost. In any event, the estimated costs do not change significantly using a $600 estimate, as noted in the Bureau's Regulatory Flexibility Analysis below.

[138] (350 *486) = $170,000 (rounded to the nearest thousand).

loan will not be consummated). In outreach prior to the proposal stage, market participants, including a large bank, representatives from a national community banking trade association, and a large independent mortgage bank[139] told the Bureau that, in cases where loans are consummated, copies of appraisals that are ordered are provided to consumers 100 percent of the time. Indeed, GSEs also generally require that, as a condition of eligibility for their purchase of a loan, copies of appraisals be provided to consumers promptly upon completion but no later than three days before consummation.[140] The Bureau therefore believes that for covered HPML first lien transactions, the requirement to provide copies in the rule imposes no additional costs; any cost due to providing copies for the small proportion of first lien transactions that do not currently obtain and provide copies of appraisals is estimated not to be significant. The only other costs of providing copies of the appraisals would be for the 2,000 new appraisals in subordinate lien transactions that the Bureau estimates would be caused by the rule on an annual basis. As noted in the PRA section of the final rule, the time to send the copy can be assumed to be part of the 15 minutes of time needed on average to review the appraisal. Given the number of extra copies that would need to be provided, and the provision in the final rule that allows these copies to be provided electronically based upon consent under the E-Sign Act, the Bureau believes that this cost is not significant.

As noted above, the Bureau assumes that costs of many of the new first appraisals would be borne directly by the consumers. This increase in costs charged to HPML borrowers could deter some consumers from agreeing to HPMLs. In these cases, however, creditors could agree to fold the appraisal cost into the cost of the loan. To the extent consumers would still be

[139] Interviews conducted on May 15, 2012 and May 24, 2012.
[140] Fannie Mae Selling Guide, "Appraiser Independence Requirements" (Oct. 15, 2010) (Part III), available at https://www.fanniemae.com/content/fact_sheet/air.pdf; Freddie Mac, Single Family Seller/Servicer Guide, Vol. 1, Exhibit 35, Appraiser Independence Requirements (October 15, 2010) (same).

deterred from borrowing, creditors also could waive the cost of the appraisal and absorb it, or otherwise reduce origination fees.

Costs per institution or loan officer. Aside from the per-loan costs just described, the Bureau has estimated that each institution would incur the one-time cost of reviewing the regulation, and one-time training costs for loan officers to become familiar with the provisions of the rule.[141]

Potential Costs of the Rule to Consumers

The direct pecuniary costs to consumers that would be imposed by the rule can be calculated as the incremental cost of having a full interior appraisal instead of using another valuation method for the relatively small subset of covered HPML transactions (a few thousand annually as discussed above) where an appraisal is not currently performed. As described above, the Bureau believes that consumers would pay directly for all new first appraisals – but not the new second appraisals that would be required because of a recent resale of the property – for a total of 3,794 new first appraisals per year. Assuming the consumer pays $350 for an appraisal

[141] As stated in the proposal, the Bureau estimates that on average one lawyer and a variable number of compliance officers at each institution will review the regulation for 1.5 hours each person. Compliance officer review is assumed to vary by size and type of the institution, and it is assumed that in some cases there is no compliance officer review: one compliance officer at each independent mortgage bank; two compliance officers at each depository institution larger than $10 billion in assets; and half a compliance officer (on average) at each depository institution smaller than $10 billion in assets. Total hourly labor costs are estimated to be: $116.08 for attorneys and $52.04 for compliance officers. Actual review time will vary by institution. At some institutions that do not originate non-QM HPMLs, review time may be lower as lawyers and compliance officers may review secondary trade press or other free sources of information. By contrast, for those institutions that originate non-QM HPMLs, the review time may be greater as it may include activities to prepare for implementation, such as training. As also stated in the proposal, the Bureau estimates that on average an additional 0.5 hours of training time will be added to regular training programs for each loan officer. Here again, training time will vary depending on whether the officer is involved in origination of non-QM HPMLs. One community bank commenter stated that the estimate in the proposal of 30 minutes for training time was too low, but did not explain the amount of time it believed would be required for training. Training time per officer may be lower than average for many loan officers to the extent they do not or are not likely to originate non-QM HPMLs, and closer to or potentially more than average in some cases for those who do or may originate such loans (because those officers would need to be trained on how to comply with the rule, rather than simply alerted to its existence). Finally, the Bureau also believes that as part of routine software updates, creditors may make adjustments to software systems to ensure compliance with this rule; the Bureau does not believe these adjustments would impose significant additional costs beyond the existing routine upgrade processes.

that would not otherwise have been conducted, versus $5 for an alternative valuation, gives a total direct costs to consumers of 3,794 * ($350-$5) = $1,308,930 (rounded to the nearest thousand).

Potential Reduction in Access by Consumers to Consumer Financial Products or Services

Incremental costs in covered HPML transactions that would not otherwise have a full-interior appraisal could reduce consumers' access to non-QM HPMLs. However, the impact on access to credit is probably negligible. Any costs that derive from the additional underwriting requirements incurred under the rule are likely to be very small. What matters, for both first and subordinate lien loans, are the incremental costs from the difference between the full-interior appraisal and alternative valuation method costs. These only arise in the fraction of HPMLs where use of the interior appraisal is not already accepted practice. For first liens, full interior inspection appraisals are common industry practice: passing the cost of appraisals on to consumers is current industry practice, and consumers appear to accept the appraisal fee. The interior appraisal requirement therefore is unlikely to cause a significant adverse effect on consumers' access to this kind of credit. Furthermore, these costs may also be rolled into the loan, up to LTV ratio limits, so buyers are unlikely to face short-term liquidity constraints that prevent purchasing the home. The impact of the rule on the volume of non-QM HPMLs originated may be relatively greater for subordinate liens because in these transactions the rule would impose an interior appraisal practice that is not as widespread currently, and also because the cost of a full interior appraisal is a larger proportion of the loan amount (because subordinate lien loans are typically lower in amount than first lien loans). However, the number of subordinate lien HPMLs that will be covered by the rule will be small to begin with, excluding qualified mortgages; any changes in non-QM HPML subordinate lien transaction volume may be mitigated by consumers rolling the appraisal costs into the loan or the consumer and the creditor splitting the incremental cost of the full-interior appraisal if it is profitable for the creditor to do so.

Significant Alternatives Considered

In determining what level of review by creditors should be required for full interior appraisals related to HPMLs, two alternatives were considered in developing the proposed rule. One alternative considered was to require a full technical review of the appraisal that would comply with USPAP Standard 3 (USPAP3). Such a requirement, however, would add substantially to the cost of each appraisal, as a USPAP3-compliant review can cost nearly as much as a full interior appraisal. Another alternative was to require creditors to have USPAP3-compliant reviews conducted on a sample of the appraisals carried out on properties related to an HPML. Reviewing a sample of appraisals, however, would be most useful for creditors making a large number of HPMLs and employing the same appraisers for a large number of those loans. Given the small number of HPMLs made each year, the value of sampling appraisals for full USPAP3 review is likely to be small.

In addition to the exemptions that were adopted in the final rule, based upon its review of comments discussed in the section-by-section analysis above, the Agencies also considered possible exemptions from the final rule for “streamlined” refinance programs (such as programs designed by certain government agencies and government-sponsored enterprises that do not require appraisals), and loans of lower dollar amounts, and clarification on application of the rule to loans secured by certain property types. As discussed in the section-by-section analysis, however, the Agencies did not adopt these exemptions or clarifications in the final rule and instead intend to publish a supplemental proposal to request additional comment on these issues.

Finally, the Agencies considered alternatives to the scope of the second appraisal requirement for HPMLs on properties being resold within 180 days. With respect to what price increase would trigger this requirement, in addition to the approach adopted in the final rule, the Agencies also considered whether the trigger should be any amount greater than zero, an increase of 10 percent regardless of the number of days between 0 and 180 days since the acquisition, or an increase of 20 percent regardless of the number of days between 0 and 180 days since the acquisition. For the reasons outlined in the section-by-section analysis above, the Agencies determined that setting staggered price increase thresholds – more than 10 percent for properties acquired within 90 days and more than 20 percent for properties acquired within 91 and 180 days – was more appropriate. In addition, the Agencies considered providing no exemption from the second appraisal requirement for loans on properties located in rural areas (as proposed), or providing an exemption for loans on properties in rural areas defined using combinations of urban influence codes (UICs). For the reasons outlined in the section-by-section analysis above, the Agencies determined that an exemption was appropriate for HPMLs secured by properties located in certain UICs, as discussed in the section-by-section analysis of § 1026.35(c)(4)(vii)(H) above. .

Impact of the Rule on Depository Institutions and Credit Unions With $10 Billion or Less in Total Assets, As Described in Section 1026[142]

Depository institutions and credit unions with $10 billion or less in assets would experience the same types of impacts as those described above. The impact on individual institutions would depend on the mix of mortgages that these institutions originate, the number

[142] Approximately 50 banks with under $10 billion in assets are affiliates of large banks with over $10 billion in assets and subject to Bureau supervisory authority under Section 1025. However, these banks are included in this discussion for convenience.

of loan officers that would need to be trained, and the cost of reviewing the regulation. The Bureau estimates that these institutions originated 151,000 HPML loans in 2011. Assuming the mix of purchase money, refinancings, and subordinate lien mortgages, and the proportion of loans exempt as qualified mortgages, was the same at these institutions as for the industry as a whole, the Bureau estimates that the rule will require these institutions to have 1,966 full interior appraisals conducted for transactions that would otherwise not have a full-interior appraisal, and 252 new second full-interior appraisal (as is be required by § 1026.35(c)(4)), for a total of 2,218 appraisals. As noted above, these estimates are derived without subtracting some of the loans that are exempt from the overall rule. These estimates therefore are conservative, given that these exemptions collectively apply to a significant number of loans. The Bureau believes that the impact on each creditor under $10 billion is substantially the same as for the broader group of creditors described above. In particular, based upon analysis of the same data sources described above, the Bureau has determined the under $10 billion creditors have the same cost per loan and similar one-time and ongoing burdens, with the specific differences described above.

Impact of the Final Rule on Consumers in Rural Areas

The Bureau does not anticipate that the final rule will have a unique impact on consumers in rural areas. The Bureau does not believe that requiring one interior USPAP-compliant appraisal for a covered HPML on a rural property will have a significantly greater impact than the same requirement for a covered HPML on a non-rural property.[143] Further, the final rule exempts these rural transactions from the requirement to obtain a second appraisal on the property. Therefore, the cost of creditor compliance with the second appraisal requirement

[143] Despite receiving some comments requesting an exemption from the entire rule for rural HPMLs, the Agencies have not received nationally-representative data indicating that the cost of first appraisals for HPMLs would be disproportionately difficult to incur in rural transactions.

(including due diligence) will not be present for these transactions. For these reasons, explained in more detail below, the Bureau does not anticipate the final rule will have a unique or disproportionate impact on consumers in rural areas.

As in the section 1022 analysis in the proposal, the Bureau continues to conclude that there would be no unique impact on rural consumers of the requirement to obtain the first appraisal. For first lien transactions, conditional on taking out a mortgage, rural consumers may take out first lien HPMLs at a higher rate than non-rural consumers. Such a difference between rural and non-rural rates of first lien HPMLs does not have a unique impact on rural consumers, however, because the rule does not alter existing industry practice with respect to appraisals for most first lien transactions. For subordinate lien transactions, conditional on taking out a mortgage, in 2010 the proportion of subordinate liens that were HPMLs were roughly the same for consumers in rural areas as in non-rural areas, as illustrated in Table 2 of the proposal. In addition, HMDA data for 2011 indicates the proportion of subordinate liens in rural areas that were HPMLs (6.77 percent) was lower than the proportion for non-rural areas (8.53 percent). Thus, even though the rule may have a greater impact on subordinate lien HPML transactions because appraisals are less common currently for these transactions, rural consumers' subordinate liens appear no more likely to be HPMLs than non-rural consumers, based upon the recent HMDA data. As a result, there is no unique or disproportionate impact on rural consumers in subordinate lien transactions either.

With respect to the second appraisal requirement for certain transactions involving flips, the Bureau believes that flips occur at the same rate in rural areas as in non-rural areas. The second appraisal requirement will not have any impact on consumers engaging in transactions on properties in rural areas, however, because they are exempt from the second appraisal requirement.[144] As discussed in the preamble to the final rule, based upon comments received and further analysis, the Agencies have determined that there is a sufficient basis for concern over availability of appraisers in rural areas to conduct a second appraisal on rural HPML transactions, and consequently some concern over credit availability if the second appraisal requirement were applied to these transactions. The Agencies therefore have exempted these transactions from the second appraisal requirement. This determination in the final rule is based upon a broader consideration of appraiser availability, as well as other factors discussed in the section-by-section analysis above, than the Bureau considered in its section 1022 analysis in the proposal stage. In its section 1022 analysis in the proposal, the Bureau concluded that sufficient appraisers likely would be available for a property if there were two active certified and licensed appraisers on the National Appraiser Registry in the same or adjacent county. After reviewing a number of industry comments summarized in the section-by-section analysis above, however, the Agencies concluded that this approach was too narrow. The existence of an appraiser on the registry did not necessarily guarantee that the appraiser was available, or if they were, that they would be competent or charging a reasonable fee for the transaction. As discussed in more detail in the section-by-section analysis above, when the Agencies considered more broadly whether five appraisers were available within 50 miles, the potential for appraiser availability issues grew more apparent. This broader approach was viewed as necessary, to account for the fact that one or more of the active appraisers in the registry results for a given property may not be available or appropriate for the transaction.

VI. Regulatory Flexibility Act

[144] If rural consumers had been subject to the additional appraisal requirement for transactions in rural areas, then this requirement may also have had a disproportionate impact on consumers in rural areas because significantly more rural first lien mortgage transactions were HPMLs according to 2010 HMDA data described in Table 2 of the proposal.

Board

The Board prepared an initial regulatory flexibility analysis as required by the Regulatory Flexibility Act (RFA) (5 U.S.C. 601 et seq.) (RFA) in connection with the proposed rule. The regulatory flexibility analysis otherwise required under section 604 of the RFA is not required if an agency certifies, along with a statement providing the factual basis for such certification, that the rule will not have a significant economic impact on a substantial number of small entities. 5 U.S.C. 604, 605(b). The final rule covers certain banks, other depository institutions, and non-bank entities that extend higher-risk mortgage loans to consumers. The Small Business Administration (SBA) establishes size standards that define which entities are small businesses for purposes of the RFA.[145] The size standard to be considered a small business is: $175 million or less in assets for banks and other depository institutions; and $7 million or less in annual revenues for the majority of nonbank entities that are likely to be subject to the final rule. Based on its analysis and for the reasons stated below, the Board believes that this final rule will not have a significant economic impact on a substantial number of small entities.[146]

A. Reasons for the Final Rule

Section 1471 of the Dodd-Frank Act establishes a new TILA section 129H, which sets forth appraisal requirements applicable to "higher-risk mortgages." The Act generally defines "higher-risk mortgage" as a closed-end consumer loan secured by a principal dwelling with an APR that exceeds the APOR by 1.5 percent for first-lien loans, 2.5 percent for first-lien jumbo loans, or 3.5 percent for subordinate-liens. The definition of higher-risk mortgage in new TILA

[145] U.S. Small Business Administration, Table of Small Business Size Standards Matched to North American Industry Classification System Codes, available at
http://www.sba.gov/sites/default/files/files/Size_Standards_Table.pdf

[146] The Board notes that for purposes of its analysis, the Board considered all creditors to which the final rule applies. The Board's Regulation Z at 12 CFR 226.43 applies to a subset of these creditors. *See* § 226.43(g).

section 129H expressly excludes qualified mortgages, as defined in TILA section 129C, as well as reverse mortgage loans that are qualified mortgages as defined in TILA section 129C.

Specifically, new TILA section 129H does not permit a creditor to extend credit in the form of a "higher-risk mortgage" to any consumer without first:

- Obtaining a written appraisal performed by a certified or licensed appraiser who conducts a physical property visit of the interior of the property.
- Obtaining an additional appraisal from a different certified or licensed appraiser if the purpose of the higher-risk mortgage loan is to finance the purchase or acquisition of a mortgaged property from a seller within 180 days of the purchase or acquisition of the property by that seller at a price that was lower than the current sale price of the property. The additional appraisal must include an analysis of the difference in sale prices, changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale.
- Providing the applicant, at the time of the initial mortgage application, with a statement that any appraisal prepared for the mortgage is for the sole use of the creditor, and that the applicant may choose to have a separate appraisal conducted at the applicant's expense.
- Providing the applicant with one copy of each appraisal conducted in accordance with TILA section 129H without charge, at least three (3) days prior to the transaction closing date.

Section 1400 of the Dodd-Frank Act requires that final regulations to implement these provisions be issued no later than January 21, 2013. The Agencies are issuing the final rule to fulfill their statutory duty to implement the appraisal provisions added in new TILA section 129H.

B. Statement of Objectives and Legal Basis

The **SUPPLEMENTARY INFORMATION** above contains this information. As discussed above, the legal basis for the final rule is new TILA section 129H(b)(4). 15 U.S.C. 1639h(b)(4). New TILA section 129H was established by section 1471 of the Dodd-Frank Act.

C. Summary of Issues Raised by Commenters

In the proposed rule to implement the appraisal provisions in new TILA section 129H, the Board sought information and comment on any costs, compliance requirements, or changes in operating procedures arising from the application of the rule to small institutions. The Board received comments from various industry representatives, including banks, credit unions, and the trade associations that represent them. As discussed in the S**UPPLEMENTARY INFORMATION** above, the commenters asserted that compliance with the proposed rule would have a disproportionate impact on small entities and cited concerns about the utility and expense of requiring these entities to comply with all or some of the rule's requirements. These comments, however, did not contain specific information about costs that will be incurred or changes in operating procedures that will be required for compliance.

In general, the commenters discussed the impact of statutory requirements rather than any impact that the proposed rules themselves would generate. Moreover, the Agencies have reduced the compliance burden in the final rule by adding exemptions from both the written appraisal and the additional written appraisal requirements. Thus, the Board continues to believe that the final rule will not have a significant impact on a substantial number of small entities.

D. Description of Small Entities to which the Rules Apply

The final rule applies to creditors that make HPMLs subject to 12 CFR 1026.35(c).[147] To estimate the number of small entities that will be subject to the requirements of the rule, the Board is relying primarily on data provided by the Bureau.[148] According to the data provided by the Bureau, approximately 3,466 commercial banks, 373 savings institutions, 3,240 credit unions, and 2,294 non-depository institutions are considered small entities and extend mortgages, and therefore are potentially subject to the final rule.

Data currently available to the Board are not sufficient to estimate how many small entities that extend mortgages will be subject to 12 CFR 1026.35(c), given the range of exemptions from the rules, including the exemption for qualified mortgages. Further, the number of these small entities that will make HPMLs subject to 12 CFR 1026.35(c) in the future is unknown.

D. Projected Reporting, Recordkeeping and Other Compliance Requirements

The compliance requirements of the final rule are described in detail in the **SUPPLEMENTARY INFORMATION** above.

The final rule generally applies to creditors that make HPMLs subject to 12 CFR 1026.35(c), which are generally mortgages with an APR that exceeds the APOR by a specified percentage, subject to certain exceptions. The final rule generally requires 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 creditor is required to determine whether it extends HPMLs subject to 12 CFR 1026.35(c); if so, the creditor must analyze the regulations. The creditor must establish

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[147] As discussed in the **SUPPLEMENTARY INFORMATION** above, the Agencies in the final rule are referring to “higher-risk mortgages” as HPMLs subject to 12 CFR 1026.35(c) in order to use terminology consistent with that already used in Regulation Z.

[148] *See* the Bureau’s Regulatory Flexibility Analysis.

procedures for identifying mortgages subject to the new appraisal requirements. A creditor making a HPML subject to 12 CFR 1026.35(c) must obtain a written appraisal performed by a certified or licensed appraiser who conducts a physical property visit of the interior of the property. Creditors seeking a safe harbor for compliance with this requirement must

- Order that the appraiser perform the written appraisal in conformity with the USPAP and title XI of the FIRREA, and any implementing regulations, in effect at the time the appraiser signs the appraiser's certification;
- Verify through the National Registry that the appraiser who signed the appraiser's certification was a certified or licensed appraiser in the State in which the appraised property is located as of the date the appraiser signed the appraiser's certification;
- Confirm that the elements set forth in appendix N to this part are addressed in the written appraisal; and
- Have no actual knowledge to the contrary of facts or certifications contained in the written appraisal.

A creditor must also determine whether it is financing the purchase or acquisition of a mortgaged property by a consumer from a seller (1) within 90 days of the seller's acquisition of the property for a resale price that exceeds the seller's acquisition price by more than 10 percent; or (2) 91 to 180 days of the seller's acquisition of the property for a resale price that exceeds the seller's acquisition price by more than 20 percent. If so, the creditor must obtain an additional appraisal of the property and confirm that the additional appraisal meets the requirements of the first appraisal. The creditor also must ensure that the additional appraisal includes an analysis of the difference in sale prices, changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale.

Creditors extending HPMLs subject to 12 CFR 1026.35(c) also must design, generate, and provide a new notice to applicants. Specifically, within three business days of application, a creditor must provide a disclosure that informs consumers of the purpose of the appraisal, that the creditor will provide the consumer with a copy of any appraisal, and that the consumer may choose to have a separate appraisal conducted at the expense of the consumer. In addition, creditors making HPMLs subject to 12 CFR 1026.35(c) must provide the consumer with a copy of each appraisal conducted at least three business days prior to closing and develop systems for that purpose.

The Board believes that certain factors will mitigate the economic impact of the final rule. First, the Board believes that only a small number of loans will be affected by the final rule. For example, according to HMDA data, less than four percent of first-lien home purchase mortgage loans in 2010 or 2011 would potentially be subject to the appraisal requirements of 12 CFR 1026.35(c).[149] Moreover, most home purchase loans do not involve properties that were previously purchased within 180 days and therefore would not require an additional written appraisal. In addition, based on outreach, the Board believes that many creditors are already obtaining written appraisals performed by certified or licensed appraisers who conduct a physical property visit of the interior of the property. Creditors may be obtaining such appraisals pursuant to other requirements, such as of FIRREA title XI or the FHA Anti-Flipping Rule, or they may be obtaining the appraisals voluntarily.

Because of the small number of transactions affected, the Board believes that the final rule is unlikely to have a significant economic impact on a substantial number of small entities.

E. Identification of Duplicative, Overlapping, or Conflicting Federal Regulations

[149] This estimate does not account for exemptions provided in the final rule.

The Board has not identified any Federal statutes or regulations that would duplicate, overlap, or conflict with the final rule. The final rule will work in conjunction with the existing requirements of FIRREA title XI and its implementing regulations.

F. Discussion of Significant Alternatives

As described in the **SUPPLEMENTARY INFORMATION**, above, the Board has sought to minimize the economic impact on small entities in several ways. First, the final rule provides exemptions from both the written appraisal and the additional written appraisal requirements, and provides creditors with a safe harbor for determining that an appraiser has met certain specified requirements. The final rule also replaces the term “higher-risk mortgage loan” with “higher-priced mortgage loan” in order to use terminology consistent with that already used in Regulation Z. Moreover, the final rule seeks to reduce burden by providing that the disclosure required at application may be fulfilled by compliance with the disclosure requirement in Regulation B, 12 CFR 1002.14(a)(2). Lastly, the final rule seeks to reduce burden by allowing a creditor subject to the additional appraisal requirement under TILA section 129H(b)(2) to obtain an appraisal that contains the analysis required in TILA section 129H(b)(2)(A) only to the extent that needed information is known. 15 U.S.C. 1639h(b)(2).

Bureau

The Regulatory Flexibility Act (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.[150]

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[150] For purposes of assessing the impacts of the final rule on small entities, “small entities” is defined in the RFA to include small businesses, small not-for-profit organizations, and small government jurisdictions. 5 U.S.C. 601(6). A “small business” is determined by application of Small Business Administration regulations and reference to the

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.[151] A FRFA is not required because this rule will not have a significant economic impact on a substantial number of small entities.

A. Summary of Final Rule

The empirical approach to calculating the impact that the regulation has on small entities subject to the final rule follows the methodology, and uses the same data, as the above analysis conducted under Section 1022 of the Dodd-Frank Act. The impact analysis focuses on the economic impact of the final rule, relative to a pre-statute baseline, for small depository institutions (DIs) and non-depository independent mortgage banks (IMBs), also described in this impact analysis as non-DIs. The Small Business Administration classifies DIs (commercial banks, savings institutions, credit unions, and other depository institutions) as small if they have no more than $175 million in assets, and classifies other real estate credit firms (including non-DIs) as small if they have no more than $7 million in annual revenues.[152]

The final rule implements section 1471 of the Dodd-Frank Act, which establishes appraisal requirements for HPMLs that are not otherwise exempt under the final rule. Under the exemptions in the final rule, the final rule does not apply qualified mortgages as defined in the Bureau's 2013 ATR Final Rule, transactions secured by a new manufactured home, transactions secured by a mobile home, boat, or trailer, transactions to finance the initial construction of a dwelling, temporary bridge loans with a term of 12 months or less, or reverse mortgages.

North American Industry Classification System (NAICS) classifications and size standards. 5 U.S.C. 601(3). A "small organization" is any "not-for-profit enterprise which is independently owned and operated and is not dominant in its field." 5 U.S.C. 601(4). A "small governmental jurisdiction" is the government of a city, county, town, township, village, school district, or special district with a population of less than 50,000. 5 U.S.C. 601(5).

[151] 5 U.S.C. 609.

[152] 13 CFR Ch. 1.

Consistent with the statute, the final rule allows a creditor to make a covered HPML only if the following conditions are met:

- The creditor obtains a written appraisal;
- The appraisal is performed by a certified or licensed appraiser; and
- The appraiser conducts a physical property visit of the interior of the property.

In addition, as required by the Act, the final rule requires a creditor originating a covered HPML to obtain an additional written appraisal, at no cost to the borrower, if certain conditions are met, unless a transaction falls into one of the exemptions from this requirement in the rule (exemptions are described in § 1026.35(c)(4)(vii). The following conditions trigger this requirement:

- The HPML will finance the acquisition of the consumer’s principal dwelling;
- The seller selling what will become the consumer’s principal dwelling acquired the home within 180 days prior to the consumer’s purchase agreement (measured from the date of the consumer’s purchase agreement); and
- The consumer is acquiring the home for a price that is more than 10 percent higher than the price at which the seller acquired the property (if the seller acquired the property within 90 days of the consumer’s purchase agreement) or more than 20 percent higher than the price at which the seller acquired the property (if the seller acquired the property within 91 to 180 days of the consumer’s purchase agreements).

The additional written appraisal, from a different licensed or certified appraiser, generally must include the following information: an analysis of the difference in sale prices (*i.e.*, the price at which the seller previously acquired the property, and the price at which the consumer agreed to acquire the property as set forth in the consumer’s purchase agreement), changes in market conditions, and any improvements made to the property between the date of the seller's previous acquisition and the consumer's agreement to acquire the property.

Finally, the rule requires creditors in covered HPML transactions to provide a standardized notice to consumers regarding the appraisal process within three days of the application, as well as a free copy of any written appraisal obtained for the transaction no later than three business days prior to consummation of the transaction (or within 30 days of determining the transaction will not be consummated).

B. Number and Classes of Affected Entities

Of the roughly 17,462 depository institutions (including credit unions) and IMBs, 12,568 are below the relevant small entity thresholds. Of the small institutions, 9,094 are estimated to have originated mortgaged loans in 2011. While loan counts exist for credit unions and HMDA-reporting DIs and IMBs, they must be projected for non-HMDA reporters. For IMBs, an accepted statistical method ("nearest neighbor matching") is used to estimate the number of these institutions that have no more than $7 million in revenues from the MCR.

Table 1. Counts of Creditors by Type.

Category	NAICS Code	Total Entities	Small Entities	Entities That Originate Any Mortgage Loans[b]	Small Entities that Originate Any Mortgage Loans
Commercial Banking	522110	6,505	3,601	6,307[a]	3,466[a]
Savings Institutions	522120	930	377	922[a]	373[a]
Credit Unions[c]	522130	7,240	6,296	4,178[a]	3,240[a]
Real Estate Credit[d e]	522292	2,787	2,294	2,787	2,294[a]
Total		17,462	12,568	14,194	9,373

Source: 2011 HMDA, Dec 31, 2011 Bank and Thrift Call Reports, Dec 31, 2011 NCUA Call Reports, Dec 31, 2011 NMLSR Mortgage Call Reports.

[a] For HMDA reporters, loan counts from HMDA 2011. For institutions that are not HMDA reporters, loan counts projected based on Call Report data fields and counts for HMDA reporters.

[b] Entities are characterized as originating loans if they make one or more loans.

[c] Does not include cooperatives operating in Puerto Rico. The Bureau has limited data about these institutions, which are subject to Regulation Z, or their mortgage activity.

[d] NMLSR Mortgage Call Report ("MCR") for 2011. All MCR reporters that originate at least one loan or that have positive loan amounts are considered to be engaged in real estate credit (instead of purely mortgage brokers). For institutions with missing revenue values, the probability that institution was a small entity is estimated based on the count and amount of originations and the count and amount of brokered loans.

[e] Data do not distinguish nonprofit from for-profit organizations, but Real Estate Credit presumptively includes nonprofit organizations.

C. Analysis

Although most DIs and non-DIs are affected by the final rule, the final rule does not have a significant impact on a substantial number of small entities, as is demonstrated by the burden estimates for small institutions calculated below. For each institution the cost of compliance is calculated and then divided by a measure of revenue. For DIs, revenue is obtained from the appropriate call report. For non-DIs, the frequency of HPMLs is not available in the MCR. However, data available in HMDA shows that the proportion of HPMLs in a non-DI's originations does not vary by origination volume. As such, HMDA data is used in lieu of the MCR data to calculate costs of compliance with the final rule.

The creditors will incur one-time costs of review, as described in the analysis under section 1022 above, and ongoing costs, proportional to the volume of HPMLs originated, and also as described in the section 1022 analysis above.

The Bureau estimates that 85 percent of the creditors affected are going to have one-time costs of less than $300.[153] Using an alternative metric, 85 percent of the creditors have a ratio of one-time costs to their revenue of less than 0.1 percent.[154]

For small DIs, Table 2 reports various statistics for the estimated annual cost of compliance with the final rule as a percentage of revenues using conservative assumptions. The assumptions underlying the Bureau's estimates are explained in the table and are generally discussed in more detail in the Section 1022(b)(2) analysis. The table shows that 85 percent of the small DIs and credit unions that originate any HPMLs have costs of significantly less than one percent of the revenue. This stays the same when the creditors are separated into types.[155]

[153] Banks, saving institutions, and credit unions all have comparatively lower numbers. For the small IMBs, 85 percent are going to have one-time setup costs of less than $445.

[154] Even for the small IMBs this ratio is less than 1 percent for 85 percent of the IMBs. The numbers are much lower for the other types of creditors.

[155] The final rule would not have a significant impact on a substantial number of small DIs, even if the cost of appraisals were assumed to be significantly higher than the average cost – such as at $600, as conservatively assumed in the proposal based upon the state with the highest median – and even if the analysis did not assume any HPMLs would meet the criteria for exemptions in the final rule. The switches from $350 to $600 for appraisal cost and from non-QM to all HPMLs would increase the percentages in the table approximately by a factor of 20. However, even then the impact remains well within 3 percent for 85 percent of the institutions.

Table 2. Recurring Costs of Rule as a Share of Revenue by Type of Creditor (85th Percentile).

	Small HPML Originators	85th Percentile
All Institutions	4461	<0.01%
Banks	3006	<0.01 %
Thrifts	310	<0.01 %
Credit Unions	1145	<0.01%

Assumptions: Costs per-transaction and per-loan officer are as described in the section 1022(b)(2) analysis. These include but are not limited to the following: Full-interior appraisals – whether first or second – cost $350, alternative valuations cost $5. In the absence of the rule, the probability of a full-interior appraisal for a transaction is 95 percent for purchase-money transactions, 90 percent for refinance transactions, and 5 percent for subordinate-lien mortgages. The proportion of resales within 180 days is 5 percent, without regard to difference in price. Costs of the first full interior appraisal are passed on completely to consumers. The review of the appraisal upon receipt takes 15 minutes of loan officer time. The Bureau also includes 15 minutes of loan officer time per loan to estimate whether the transaction is a flip.

The Bureau also has analyzed the data for IMBs separately. Most IMBs are small, and the Bureau does not possess the data on the revenues of approximately 700 of those. As with the DIs and credit unions, the effects of the rule are insignificant. Out of the 1,325 small IMBs that originate any HPMLs, and for whom the Bureau possesses revenue information, 85 percent of the IMBs have costs below 0.30 percent of the revenue, using the same cost assumptions as for the depository institutions and credit unions.[156] The exemptions from the rule and from its second appraisal requirement significantly reduce the number of HPMLs subject to these requirements, almost tenfold. For the remaining HPMLs that are covered by the rule, such as non-QM HPMLs, because many of the costs imposed by the final rule are likely to be passed on to consumers, this may result in a decrease in demand for those loans (such as non-QM HPMLs).

[156] The final rule would not have a significant impact on a substantial number of small IMBs, even if the cost of appraisals were assumed to be significantly higher than the average cost – at $600, as conservatively assumed in the proposal – and even if the analysis did not assume any HPMLs would meet the criteria for exemptions in the final rule. The switches from $350 to $600 for appraisal cost and from non-QM to all HPMLs would increase the percentages in the table approximately by a factor of 20. However, even then the impact remains well within 3 percent for 85 percent of the institutions

However, any possible decrease in non-QM HPML volume is likely to be negligible. For both first-lien and subordinate-lien HPMLs, the principal increase in cost to consumers is the difference in costs between the full-interior appraisal and any alternative valuation method costs; some other costs imposed by the rule, such as creditor labor costs discussed in the section 1022(b)(2) analysis above, and the cost of providing required disclosures, also may be reflected in increases in the fees or rates charged in a class of loans. These charges are unlikely to exceed $600. For first lien transactions, full interior inspections are common industry practice so for the typical first lien transaction this increase in cost to consumers would be small. Furthermore, these costs may also be rolled into the loan, up to loan-to-value ratio limits, so short-term liquidity constraints for buyers are unlikely to bind. Passing the cost of appraisals on to consumers is current industry practice, and consumers appear to accept the appraisal fee, so there is unlikely to be an adverse effect on demand.

A more likely impact – albeit significantly reduced by the scope of exemptions adopted in the final rule – would be on the volume of non-QM HPMLs secured by subordinate liens because, in practice, these are the transactions on which final rule imposes a change from the status quo, and also because the cost of a full interior appraisal is a larger proportion of the loan amount to the extent subordinate lien loan amounts generally are lower than first lien loan amounts. However, changes in the volume of subordinate lien non-QM HPMLs may be mitigated by consumers rolling the appraisal costs into the loan or the consumer and the creditor splitting the incremental cost of the full-interior appraisal if it is profitable for the creditor to do so. In addition, many creditors originating subordinate lien non-QM HPMLs can offer alternative products that are not subject to the rule, such as qualified mortgages or home equity lines of credit (HELOCs). Similarly, the costs imposed on creditors are sufficiently small that they are unlikely to result in a decrease in the supply of credit.

D. Certification

Accordingly, the Director of the Consumer Financial Protection Bureau certifies that this rule will not have a significant economic impact on a substantial number of small entities.

FDIC

The RFA generally requires that, in connection with a final rulemaking, an agency prepare a final regulatory flexibility analysis that describes the impact of the final rule on small entities.[157] A regulatory flexibility analysis is not required, however, if the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities (defined in regulations promulgated by the Small Business Administration to include banking organizations with total assets of less than or equal to $175 million) and publishes its certification along with a statement providing the factual basis for such certification in the *Federal Register* together with the rule.

As of March 31, 2012, there were approximately 2,571 small FDIC-supervised banks, which include 2,410 state nonmember banks and 161 state-chartered savings banks. The FDIC analyzed the 2010 Home Mortgage Disclosure Act[158] (HMDA) dataset to determine how many loans by FDIC-supervised banks might qualify as HPMLs under section 129H of TILA, as added by section 1471 of the Dodd-Frank Act.[159] This analysis reflected that only 70 FDIC-supervised

[157] *See* 5 U.S.C. 601 *et seq*.
[158] The FDIC based its analysis on the HMDA data, as it provided a proxy for the characteristics of HPMLs. While the FDIC recognizes that fewer higher-priced loans were generated in 2010, a more historical review is not possible because the average offer price (a key data element for this review) was not added until the fourth quarter of 2009. The FDIC also recognizes that the HMDA data provides information relative to mortgage lending in metropolitan statistical areas, but not in rural areas.
[159] The FDIC notes that the exact number of small entities likely to be affected by the final rule is unknown because the FDIC lacks reliable sources for certain information.

banks originated at least 100 HPMLs, with only four banks originating more than 500 HPMLs. Further, the FDIC-supervised banks that met the definition of a small entity originated on average less than eight HPML loans each in 2010.

The three requirements[160] in the final rule that could impact small FDIC-supervised institutions most significantly are:

1. requiring an appraisal in connection with real estate financial transactions that previously did not require an appraisal,
2. mandating that the appraiser conduct a physical visit to the interior of the property, and
3. requiring a second appraisal at the lender's expense in certain situations.

As for the first potential impact, the FDIC notes that Part 323 of the FDIC Rules and Regulations[161] (Part 323) requires financial institutions to obtain an appraisal for federally related transactions unless an exemption applies. Part 323 grants an exemption to the appraisal requirement for real estate-related financial transactions of $250,000 or less. However, Part 323 requires financial institutions to obtain an appropriate evaluation that is consistent with safe and sound banking practices for such transactions. The final rule will supersede this exemption, resulting in creditors having to obtain an appraisal for an HPML transaction regardless of the transaction amount. The requirement to obtain an appraisal rather than an evaluation does not add much, if any, new burden on FDIC-supervised institutions, as they are required by Part 323 to obtain some type of valuation of the mortgaged property. The final rule merely limits the type of permissible valuation to an appraisal for HPMLs.

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[160] The requirements to provide consumers with a statement disclosing the purpose of the appraisal and to furnish consumers a copy of the appraisal without charge at least three days prior to closing should not create a significant new burden, as most FDIC-supervised institutions routinely provide required disclosures and copies of the appraisal to consumers in a timely manner.

[161] 12 CFR Part 323.

As for the second potential impact, the final rule's requirement affects a lender only to the extent that a lender must instruct the appraiser to conduct a physical visit of the interior of the mortgaged property. USPAP and title XI of FIRREA, and the regulations prescribed thereunder, do not require appraisers to perform on-site visits. Instead, USPAP requires appraisers to include a certification which clearly states whether the appraiser has or has not personally inspected the subject property. During informal outreach conducted by the Agencies, outreach participants indicated that many creditors require appraisers to perform a physical inspection of the mortgaged property. This requirement is documented in the *Uniform Residential Appraisal Report* form used as a matter of practice in the industry, which includes a certification that the appraiser performed a complete visual inspection of the interior and exterior areas of the subject property. Outreach participants indicated that requiring a physical visit of the interior of the mortgaged property added, on average, an additional cost of about $50 to the appraisal fee, which is paid by the applicant. Thus, the physical visit requirement creates a potential burden for the appraiser, not the lender, and the cost is born by the applicant.

As for the third potential impact, the final rule's requirement to conduct a second appraisal for certain transactions should not affect many FDIC-supervised banks. As previously indicated, FDIC-supervised banks that meet the definition of a small entity originated an average of less than eight HPMLs each in 2010. According to estimates provided by FHFA, about 5 percent of single-family property sales in 2010 reflected situations in which the same property had been sold within a 180-day period. This information shows that most small FDIC-supervised banks will have to obtain a second appraisal for a nominal number of transactions at the bank's expense. The estimated cost of a second appraisal is between $350 to $600.

In sum, the FDIC believes that the final rule will not have a significant economic impact on a substantial number of small entities that it regulates in light of the fact that: 1) Part 323 already requires FDIC-supervised depository institutions to obtain some type of valuation for real estate-related financial transactions; 2) the requirement of conducting a physical visit of the interior of the mortgaged property creates a potential burden for an appraiser, rather than the lender, with the cost being born by the applicant; and 3) the second appraisal requirement should affect a nominal number of transactions. Accordingly, pursuant to section 605(b) of the RFA, the FDIC certifies that the final rule will not have a significant economic impact on a substantial number of small entities.

FHFA

The final rule applies only to institutions in the primary mortgage market that originate mortgage loans. FHFA's regulated entities—Fannie Mae, Freddie Mac, and the Federal Home Loan Banks—operate in the secondary mortgage markets. In addition, these entities do not come within the meaning of small entities as defined in the Regulatory Flexibility Act. *See* 5 U.S.C. 601(6)).

NCUA

The RFA generally requires that, in connection with a final rule, an agency prepare and make available for public comment a final regulatory flexibility analysis that describes the impact of the final rule on small entities.[162] A regulatory flexibility analysis is not required, however, if the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities and publishes its certification and a short, explanatory statement in the Federal Register together with the rule. NCUA defines small entities as small

[162] *See* 5 U.S.C. 601 *et seq.*

credit unions having less than ten million dollars in assets[163] in contrast to the definition of small entities in the rules issued by the Small Business Administration (SBA), which include banking organizations with total assets of less than or equal to $175 million.

NCUA staff analyzed the 2010 Home Mortgage Disclosure Act (HMDA) dataset to determine how many loans by federally insured credit unions (FICUs) might qualify as HPMLs under section 129H of TILA.[164] As of March 31, 2012, there were 2,475 FICUs that met NCUA's small entity definition but none of these institutions reported data to HMDA in 2010. For purposes of this rulemaking and for consistency with the Agencies, NCUA reviewed the dataset for FICUs that met the small entity standard for banking organizations under the SBA's regulations. As of March 31, 2012, there were approximately 6,060 FICUs with total assets of $175 million or less. Of the FICUs which reported 2010 HMDA data, 452 reported at least one HPML. The data reflects that only three FICUs originated at least 100 HPMLs, with no FICUs originating more than 500 HPMLs, and 88 percent of reporting FICUs originating ten HPMLs or less. Further, FICUs that met the SBA's definition of a small entity originated an average four HPML loans each in 2010.[165]

As previously discussed, section 1471 of the Dodd-Frank Act[166] generally prohibits a creditor from extending credit in the form of a HPML to any consumer without first:

[163] 68 FR 31949 (May 29, 2003).
[164] NCUA based its analysis on the HMDA data, as it provided a proxy for the characteristics of HPMLs. The analysis is restricted to 2010 HMDA data because the average offer price (a key data element for this review) was not added in the HMDA data until the fourth quarter of 2009.
[165] With only a fraction of small FICUs reporting data to HMDA, NCUA also analyzed FICUs not observed in the HMDA data. Using the total number of real estate loans originated by FICUs with less than $175M in total assets, NCUA estimated the average number of HPMLs per real estate loan originated. Using this ratio to interpolate the likely number of HPML originations, the analysis suggests that small FICUs originate on average less than two HPML loans each year.
[166] Codified at section 129H of the Truth-in-Lending Act, 15 U.S.C. 1631 et seq.

- Obtaining a written appraisal performed by a certified or licensed appraiser who conducts a physical property visit of the interior of the property.
- Obtaining an additional appraisal from a different certified or licensed appraiser if the HPML finances the purchase or acquisition of a property from a seller at a higher price than the seller paid, within 180 days of the seller's purchase or acquisition. The additional appraisal must include an analysis of the difference in sale prices, changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale.
- Providing the applicant, at the time of the initial mortgage application, with a statement that any appraisal prepared for the mortgage is for the sole use of the creditor, and that the applicant may choose to have a separate appraisal conducted at the applicant's expense.
- Providing the applicant with one copy of each appraisal conducted in accordance with TILA section 129H without charge, at least three (3) days prior to the transaction closing date.

The final rule implements the appraisal requirements of section 1471 of the Dodd-Frank Act. Part 722 of NCUA's regulations[167] requires FICUs to obtain an appraisal for federally related transactions unless an exemption applies. Part 722 grants an exemption to the appraisal requirement for real estate-related financial transactions of $250,000 or less. However, part 722 requires FICUs to obtain an appropriate evaluation that is consistent with safe and sound practices for such transactions.

[167] 12 CFR part 722.

The final rule will supersede this exemption, resulting in FICUs having to obtain an appraisal for a HPML transaction regardless of the transaction amount. The requirement to obtain an appraisal rather than an evaluation does not pose a new burden to financial institutions, as they are required by part 722 to obtain some type of valuation of the mortgaged property. The final rule merely limits the type of permissible valuations to an appraisal for HPMLs.

The final rule's requirement to conduct a physical visit of the interior of the mortgaged property potentially adds an additional burden to the appraiser. The USPAP and title XI of FIRREA and the regulations prescribed thereunder do not require appraisers to perform on-site visits. Instead, USPAP requires appraisers to include a certification which clearly states whether the appraiser has or has not personally inspected the subject property. During informal outreach conducted by the Agencies, outreach participants indicated that many creditors require appraisers to perform a physical inspection of the mortgaged property. This requirement is documented in the *Uniform Residential Appraisal Report* form used as a matter of practice in the industry, which includes a certification that the appraiser performed a complete visual inspection of the interior and exterior areas of the subject property. Outreach participants indicated that requiring a physical visit of the interior of the mortgaged property added on average an additional cost of about $50 to the appraisal fee, which is paid by the applicant.

In light of the fact that few loans made by FICUs would qualify as HPMLs, the fact that many creditors already require that an appraiser conduct an interior inspection of mortgage collateral property in connection with an appraisal; the fact that requiring an interior inspection would add a relatively small amount to the cost of an appraisal; and the various exemptions and exclusions from the requirements provided in the rule, NCUA believes the final rule will not have a significant economic impact on small FICUs.

For the reasons provided above, NCUA certifies that the final rule will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order to adhere to fundamental federalism principles. This final rule applies to Federally insured credit unions and will not have a substantial direct effect on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the Executive Order.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

NCUA has determined this final rule will not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Public Law 105-277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996[168] (SBREFA) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by Section 551 of the

[168] Pub. L. 104–121, 110 Stat. 857 (1996).

Administrative Procedure Act.[169] NCUA does not believe this final rule is a "major rule" within the meaning of the relevant sections of SBREFA. NCUA has submitted the rule to the Office of Management and Budget (OMB) for its determination.

OCC

Pursuant to section 605(b) of the Regulatory Flexibility Act, 5 U.S.C. 605(b) (RFA), the regulatory flexibility analysis otherwise required under section 603 of the RFA is not required if the agency certifies that the final rule will not, if promulgated, have a significant economic impact on a substantial number of small entities (defined for purposes of the RFA to include banks, savings institutions and other depository credit intermediaries with assets less than or equal to $175 million[170] and trust companies with total assets of $7 million or less) and publishes its certification and a short, explanatory statement in the Federal Register along with its final rule.

Section 1471 of the Dodd-Frank Act establishes a new TILA section 129H, which sets forth appraisal requirements applicable to higher-priced mortgage loans. A "higher-priced mortgage" generally is a closed-end consumer loan secured by a principal dwelling with an APR that exceeds the APOR by 1.5 percent for first-lien loans with a principal amount below the conforming loan limit, 2.5 percent for first-lien jumbo loans, or 3.5 percent for subordinate-liens. The definition of higher-priced mortgage loan expressly excludes qualified mortgages, as defined in TILA section 129C, as well as reverse mortgage loans that are qualified mortgages as defined in TILA section 129C.

[169] 5 U.S.C. 551.

[170] "A financial institution's asset are determined by averaging assets reported on its four quarterly financial statements for the preceding year." See footnote 8 of the U.S. Small Business Administration's Table of Size Standards.

Specifically, section 129H does not permit a creditor to extend credit in the form of a higher-priced mortgage loan to any consumer without first:

- Obtaining a written appraisal performed by a certified or licensed appraiser who conducts a physical property visit of the interior of the property.
- Obtaining an additional written appraisal from a different certified or licensed appraiser if the purpose of the higher-risk mortgage loan is to finance the purchase or acquisition of a mortgaged property from a seller within 180 days of the purchase or acquisition of the property by that seller at a price that was lower than the current sale price of the property. The additional written appraisal must include an analysis of the difference in sale prices, changes in market conditions, and any improvements made to the property between the date of the previous sale and the current sale.
- Providing the applicant, at the time of the initial mortgage application, with a statement that any written appraisal prepared for the mortgage is for the sole use of the creditor, and that the applicant may choose to have a separate appraisal conducted at the applicant's expense.
- Providing the applicant with one copy of each appraisal conducted in accordance with TILA section 129H without charge, at least three (3) days prior to the transaction closing date.

The OCC currently supervises 1,926 banks (1,262 commercial banks, 65 trust companies, 552 federal savings associations, and 47 branches or agencies of foreign banks). We estimate that less than 1,400 of the banks supervised by the OCC are currently originating one- to four -family residential mortgage loans. Approximately 772 OCC supervised banks are small entities based on the SBA's definition of small entities for RFA purposes. Of these, the OCC estimates that 465 banks originate mortgages and therefore may be impacted by the final rule.

The OCC classifies the economic impact of total costs on a bank as significant if the total costs in a single year are greater than 5 percent of total salaries and benefits, or greater than 2.5 percent of total non-interest expense. The OCC estimates that the average cost per small bank will range from a lower bound of approximately $10,000 to an upper bound of approximately $18,000. Using the upper bound cost estimate, we believe the final rule will have a significant economic impact on three small banks, which is not a substantial number.

Therefore, we believe the final rule will not have a significant economic impact on a substantial number of small entities. The OCC certifies that the Final Rule would not, if promulgated, have a significant economic impact on a substantial number of small entities.

OCC Unfunded Mandates Reform Act of 1995 Determination

Section 202 of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1532), requires the OCC to prepare a budgetary impact statement before promulgating a rule that includes a Federal mandate that may result in the expenditure by state, local, and tribal governments, in the aggregate, or by the private sector, of $100 million or more in any one year (adjusted annually for inflation). The OCC has determined that this final rule will not result in expenditures by state, local, and tribal governments, or the private sector, of $100 million or more in any one year. Accordingly, the OCC has not prepared a budgetary impact statement.

VII. Paperwork Reduction Act

Certain provisions of this final rule contain "collection of information" requirements within the meaning of the Paperwork Reduction Act (PRA) of 1995 (44 U.S.C. 3501 *et seq.*).

Under the PRA, the Agencies may not conduct or sponsor, and a person is not required to respond to, an information collection unless the information collection displays a valid Office of Management and Budget (OMB) control number. The information collection requirements contained in this joint notice of final rulemaking have been submitted to OMB for review and approval by the Bureau, FDIC, NCUA, and OCC under section 3506 of the PRA and section 1320.11 of the OMB's implementing regulations (5 CFR part 1320). The Board reviewed the final rule under the authority delegated to the Board by OMB.

Title of Information Collection: HPML Appraisals.

Frequency of Response: Event generated.

Affected Public: Businesses or other for-profit and not-for-profit organizations.[171]

Bureau: Insured depository institutions with more than $10 billion in assets, their depository institution affiliates, and certain non-depository mortgage institutions.[172]

FDIC: Insured state non-member banks, insured state branches of foreign banks, and certain subsidiaries of these entities.

OCC: National banks, Federal savings associations, Federal branches or agencies of foreign banks, or any operating subsidiary thereof.

Board: State member banks, uninsured state branches and agencies of foreign banks.

NCUA: Federally-insured credit unions.

Abstract:

[171] The burdens on the affected public generally are divided in accordance with the Agencies' respective administrative enforcement authority under TILA section 108, 15 U.S.C. 1607.

[172] The Bureau and the Federal Trade Commission (FTC) generally both have enforcement authority over non-depository institutions for Regulation Z. Accordingly, for purposes of this PRA analysis, the Bureau has allocated to itself half of the Bureau's estimated burden for non-depository mortgage institutions. The FTC is responsible for estimating and reporting to OMB its share of burden under this proposal.

The collection of information requirements in this final rule are found in paragraphs (c)(3)(i), (c)(3)(ii), (c)(4), (c)(5), and (c)(6) of 12 CFR 1026.35. This information is required to protect consumers and promote the safety and soundness of creditors making HPMLs subject to 12 CFR 1026.35(c). This information is used by creditors to evaluate real estate collateral securing HPMLs subject to 12 CFR 1026.35(c) and by consumers entering these transactions. The collections of information are mandatory for creditors making HPMLs subject to 12 CFR 1026.35(c). The final rule requires that, within three business days of application, a creditor provide a disclosure that informs consumers of the purpose of the appraisal, that the creditor will provide the consumer a copy of any appraisal, and that the consumer may choose to have a separate appraisal conducted at the expense of the consumer (Initial Appraisal Disclosure). *See* 12 CFR 1026.35(c)(5). If a loan is a HPML subject to 12 CFR 1026.35(c), then the creditor is required to obtain a written appraisal prepared by a certified or licensed appraiser who conducts a physical visit of the interior of the property that will secure the transaction (Written Appraisal), and provide a copy of the Written Appraisal to the consumer. *See* 12 CFR 1026.35(c)(3)(i) and (c)(6). To qualify for the safe harbor provided under the final rule, a creditor is required to review the Written Appraisal as specified in the text of the rule and Appendix N. *See* 12 CFR 1026.35(c)(3)(ii).

A creditor is required to obtain an additional appraisal (Additional Written Appraisal) for a HPML that is subject to 12 CFR 1026.35(c) if (1) the seller acquired the property securing the loan 90 or fewer days prior to the date of the consumer's agreement to acquire the property and the resale price exceeds the seller's acquisition price by more than 10 percent; or (2) the seller acquired the property securing the loan 91 to 180 days prior to the date of the consumer's agreement to acquire the property and the resale price exceeds the seller's acquisition price by more than 20 percent. *See* 12 CFR 1026.35(c)(4). The Additional Written Appraisal must meet the requirements described above and also analyze: (1) the difference between the price at which the seller acquired the property and the price the consumer agreed to pay, (2) changes in market conditions between the date the seller acquired the property and the date the consumer agreed to acquire the property, and (3) any improvements made to the property between the date the seller acquired the property and the date on which the consumer agreed to acquire the property. *See* 12 CFR 1026.35(c)(4)(iv). A creditor is also required to provide a copy of the Additional Written Appraisal to the consumer. 12 CFR 1026.35(c)(6).

Comments on Proposed PRA Estimate

In the proposal, the Agencies proposed a Calculation of Estimated Burden based on the proposed requirements. The Agencies received one comment from a bank in response to the PRA estimate in the proposed rule. The commenter asserted that the Agencies' proposed PRA estimates to comply with the new requirements were understated, but the commenter did not provide alternative estimates. The Agencies recognize that the amount of time required of institutions to comply with the requirements may vary; however, the Agencies continue to believe that estimates provided are reasonable averages.

The requirements provided in the final rule are substantially similar to those provided in the proposed rule. Based upon data available to the Bureau as described in its section 1022 analysis above and in the table below, the estimated burdens allocated to the Bureau are revised from the proposal to reflect an institution count based upon updated data and reduced to reflect those exemptions in the final rule for which the Bureau has identified data. Because these data were unavailable to the other Agencies before finalizing this PRA section, the other Agencies did not adjust the calculations to account for the exempted transactions provided in the final rule. Accordingly, the estimated burden calculations in the table below are overstated.

Calculation of Estimated Burden

For the Initial Appraisal Disclosure, the creditor is required to provide a short, written disclosure within three days of application. Because the disclosure is classified as a warning label supplied by the Federal government, the Agencies are assigning it no burden for purposes of this PRA analysis.[173]

The estimated burden for the Written Appraisal requirements includes the creditor's burden of reviewing the Written Appraisal in order to satisfy the safe harbor criteria set forth in the rule and providing a copy of the Written Appraisal to the consumer. Additionally, as discussed above, an Additional Written Appraisal containing additional analyses is required in certain circumstances. The Additional Written Appraisal must meet the standards of the Written Appraisal. The Additional Written Appraisal is also required to be prepared by a certified or licensed appraiser different from the appraiser performing the Written Appraisal, and a copy of the Additional Written Appraisal must be provided to the consumer. The creditor must separately review the Additional Written Appraisal in order to qualify for the safe harbor provided in the final rule.

The Agencies estimate that respondents will take, on average, 15 minutes for each HPML that is subject to 12 CFR 1026.35(c) to review the Written Appraisal and to provide a copy of the Written Appraisal. The Agencies estimate further that respondents will take, on average, 15 minutes for each HPML that is subject to 12 CFR 1026.35(c) to investigate and verify the need

[173] The public disclosure of information originally supplied by the Federal government to the recipient for the purpose of disclosure to the public is not included within the definition of "collection of information." 5 CFR 1320.3(c)(2).

for an Additional Written Appraisal and, where necessary, an additional 15 minutes to review the Additional Written Appraisal and to provide a copy of the Additional Written Appraisal. For the small fraction of loans requiring an Additional Written Appraisal, the burden is similar to that of the Written Appraisal. The following table summarizes these burden estimates.

Estimated PRA Burden

Table 3. Summary of PRA Burden Hours for Information Collections in Final Rule

	Estimated Number of Respondents [a]	Estimated Number of Appraisals Per Respondent[174] [b]	Estimated Burden Hours Per Appraisal [c]	Estimated Total Annual Burden Hours [d] = (a*b*c)
Review and Provide a Copy of Written Appraisal				
Bureau[175],[176],[177]				
Depository Inst. > $10 B in total assets +				
Depository Inst. Affiliates	132	6.21	0.25	205
Non-Depository Inst. and Credit Unions	2,853	0.38	0.25	136[178]
FDIC	2,571	8	0.25	5,142
Board[179]	418	24	0.25	2,508
OCC	1,399	69	0.25	24,133
NCUA	2,437	6	0.25	3,656
Total	9,810			35,780
Investigate and Verify Requirement for Additional Written Appraisal				
Bureau				
Depository Inst. > $10 B in total assets +				
Depository Inst. Affiliates	132	20.05	0.25	662
Non-Depository Inst. and Credit Unions	2,853	1.22	0.25	435
FDIC	2,571	15	0.25	9,641
Board	418	24	0.25	2,508
OCC	1,399	69	0.25	24,133

[174] The "Estimated Number of Appraisals Per Respondent" reflects the estimated number of Written Appraisals and Additional Written Appraisals that will be performed solely to comply with the final rule. It does not include the number of appraisals that will continue to be performed under current industry practice, without regard to the final rule's requirements.

[175] The information collection requirements (ICs) in this final rule will be incorporated with the Bureau's existing collection associated with Truth in Lending Act (Regulation Z) 12 CFR 1026 (OMB No. 3170-0015).

[176] The burden estimates allocated to the Bureau are updated using the data described in the Bureau's section 1022 analysis above, including significant burden reductions after accounting for qualified mortgages that are exempt from the final rule, and burden reductions after accounting for loans in rural areas that are exempt from the Additional Written Appraisal requirement in the final rule.

[177] There are 153 depository institutions (and their depository affiliates) that are subject to the Bureau's administrative enforcement authority. In addition, there are 146 privately-insured credit unions that are subject to the Bureau's administrative enforcement authority. For purposes of this PRA analysis, the Bureau's respondents under Regulation Z are 135 depository institutions that originate either open or closed-end mortgages; 77 privately-insured credit unions that originate either open or closed-end mortgages; and an estimated 2,787 non-depository institutions that are subject to the Bureau's administrative enforcement authority. Unless otherwise specified, all references to burden hours and costs for the Bureau respondents for the collection under Regulation Z are based on a calculation that includes half of the burden for the estimated 2,787 non-depository institutions and 77 privately-insured credit unions.

[178] The Bureau assumes half of the burden for the IMBs and the credit unions supervised by the Bureau. The FTC assumes the burden for the other half.

[179] The ICs in this rule will be incorporated with the Board's Reporting, Recordkeeping, and Disclosure Requirements associated with Regulation Z (Truth in Lending), 12 CFR part 226, and Regulation AA (Unfair or Deceptive Acts or Practices), 12 CFR part 227 (OMB No. 7100-0199). The burden estimates provided in this rule pertain only to the ICs associated with this final rule.

NCUA	2,437	6	0.25	3,656
Total	9,810			41,035
Review and Provide a Copy of Additional Written Appraisal				
Bureau				
Depository Inst. > $10 B in total assets +				
Depository Inst. Affiliates	132	0.64	0.25	21
Non-Depository Inst. and Credit Unions	2,853	0.04	0.25	14
FDIC	2,571	1	0.25	643
Board	418	1	0.25	105
OCC	1,399	3	0.25	1,049
NCUA	2,437	0.3	0.25	183
Total	9,810			2,015

Notes:
1) Respondents include all institutions estimated to originate HPMLs that are subject to 12 CFR 1026.35(c).
2) There may be an additional ongoing burden of roughly 75 hours for privately-insured credit unions estimated to originate HPMLs that are subject to 12 CFR 1026.35(c). The Bureau will assume half of the burden for non-depository institutions and the privately-insured credit unions.

Finally, respondents must also review the instructions and legal guidance associated with the final rule and train loan officers regarding the requirements of the final rule. The Agencies estimate that these one-time costs are as follows: Bureau: 36,383 hours; FDIC: 10,284 hours; Board 3,344 hours; OCC: 19,586 hours; NCUA: 7,311 hours.[180]

The Agencies have a continuing interest in the public's opinions of our collections of information. At any time, comments regarding the burden estimate, or any other aspect of this collection of information, including suggestions for reducing the burden, may be sent to the OMB desk officer for the Agencies by mail to U.S. Office of Management and Budget, Office of Information and Regulatory Affairs, Washington, D.C., 20503, or by the internet to http://oira_submission@omb.eop.gov, with copies to the Agencies at the addresses listed in the **ADDRESSES** section of this **SUPPLEMENTARY INFORMATION**.

FHFA

The final rule does not contain any collections of information applicable to the FHFA, requiring review by the Office of Management and Budget (OMB) under the Paperwork

[180] Estimated one-time burden is calculated assuming a fixed burden per institution to review the regulations and fixed burden per estimated loan officer in training costs. As a result of the different size and mortgage activities across institutions, the average per-institution one-time burdens vary across the Agencies.

Reduction Act of 1995 (44 U.S.C. 3501, *et seq*.). Therefore, FHFA has not submitted any materials to OMB for review.

VIII. Section 302 of the Riegle Community Development and Regulatory Improvement Act

Section 1400 of the Dodd Frank Act requires this rule to take effect not later than 12 months after the date of issuance of the final rule. This rule is issued on January 18, 2013 and will become effective on January 18, 2014. Section 302 of the Riegle Community Development and Regulatory Improvement Act of 1994 ("RCDRIA") requires that, subject to certain exceptions, regulations issued by the OCC, the Board and the FDIC that impose additional reporting, disclosure, or other requirements on insured depository institutions, shall take effect on the first day of a calendar quarter which begins on or after the date on which the regulations are published in final form. This effective date requirement does not apply if the issuing agency finds for good cause that the regulation should become effective before such time. 12 USC 4802.

The OCC, the Board and the FDIC find that good cause exists to establish an effective date for this rule other than the first date of a calendar quarter, specifically January 18, 2014. This rule incorporates key definitions from, and is designed to accommodate combined disclosures with, other new mortgage-related rules being issued by the Bureau that also have effective dates on and around January 18, 2014. The consistent application of these rules will permit depository institutions to implement the systems, policies and procedures required to comply with this group of regulations in a coordinated and efficient way. In addition, insured depository institutions wishing to comply at the beginning of a calendar quarter prior to the effective date retain the flexibility to do so.