FS Regulatory Brief

CFPB Issues New Mortgage Proposals: Analysis and Next Steps

August 2012

On July 9, 2012, the Consumer Financial Protection Bureau (CFPB or Bureau) issued two Notices of Proposed Rulemaking (NPRs) to implement key residential mortgage reforms of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank).

We briefly describe these proposals below—which total almost 1400 pages combined—and will address some of their key changes in subsequent FS Regulatory Briefs. In addition, at what is still just the beginning of the expected flow of proposed mortgage-related CFPB rules, we also step back and consider how best to meet this avalanche without getting buried.

The High-Cost Mortgage and Homeownership Counseling NPR

The High-Cost Mortgage and Homeownership Counseling NPR is the comparatively "lighter" read at 292 pages. It proposes to amend Regulation Z (Truth-in-Lending Act) and Regulation X (Real Estate Settlement Procedures Act) to implement provisions of Dodd-Frank relating to the Home Ownership and Equity Protection Act (HOEPA) provisions of Regulation Z and the homeownership counseling provisions of Regulation X.

The NPR proposes to expand the types of mortgage loans that can be subject to HOEPA protections (which include increased potential liability for purchasers of HOEPA loans) and to revise and expand the factors that determine whether a mortgage is "high cost" under HOEPA. The NPR also proposes to impose additional restrictions on the loan terms that lenders may include in HOEPA mortgage loans and to implement a HOEPA pre-loan counseling requirement.

The NPR also proposes to implement other non-HOEPA Dodd-Frank pre-counseling requirements. Specifically, it would require lenders to provide borrowers a list of federally certified or approved homeownership counselors or organizations within three days of a mortgage loan application. It also would require lenders to confirm that first-time borrowers have received homeownership counseling before making a negative amortization loan to the borrower.

pwc

The Integrated Mortgage Disclosures NPR

The second NPR is an Integrated Mortgage Disclosures proposal to implement "Know Before You Owe" disclosures. Specifically, it addresses disclosures required in connection with a mortgage loan application and mortgage loan closing. This 1098-page proposal amends Regulation Z and Regulation X by combining and harmonizing existing disclosure requirements under the regulations and incorporating certain Dodd-Frank disclosure requirements.

Specifically, the NPR proposes standardized disclosure forms (with extensive instructions on compliance), which incorporate the results of the Bureau's extensive public testing and outreach efforts conducted prior to issuing this proposal. It also proposes changes to the timing of disclosures and changes to the computation of Annual Percentage Rate (APR), among other changes.

The proposed disclosures would apply to most closed-end consumer mortgages. They would not apply to home-equity lines of credit, reverse mortgages, or mortgages secured by a mobile home or by a dwelling that is not attached to the land. The NPR would exempt lenders that make five or fewer mortgages in a year.

These NPRs are only part of the CFPB's mortgage rulemaking package

Significantly, these lengthy proposals are only part of the CFPB's implementation of the Dodd-Frank provisions that apply to mortgage consumers. The Bureau also will separately propose and finalize regulations affecting mortgage servicing (yet to be proposed), loan-origination compensation (yet to be proposed), appraisals (joint agency and CFPB proposals in the works), ability-to-repay determinations and escrow (CFPB finalizing both regulations originally proposed by the Federal Reserve Board).

The CFPB summarizes each of these component parts, and projects the expected timing for each, in a Fact Sheet the Bureau released to accompany the two NPRs described above.

Under Dodd-Frank, most of these mortgage requirements become effective automatically on January 21, 2013, whether the CFPB issues final rules or not. However, the CFPB intends not to let that happen. Rather, according to statements in the Integrated Mortgage Disclosures NPR, the CFPB intends to:

- Issue a final rule prior to January 21, 2013 to exempt regulated companies from having to comply with the integrated disclosure requirements until the Bureau issues a final Integrated Mortgage Disclosures rule -- and to include a reasonable implementation period in the final rule it ultimately issues that final rule; and
- Issue final rules implementing all of the other requirements prior to January 21, 2013.[1]

What can you do now?

There are two recommended action steps that mortgage originators, servicers, settlement agents, third-party service providers, and others likely to be affected by these rules (affected companies) can take right now to ease implementation of these Dodd-Frank mortgage requirements:

1. Conduct a pre-implementation review and analysis; and,
2. Provide comments on how long a reasonable implementation period should be for the Integrated Mortgage Disclosure requirements as well as on specific concerns raised by either of the proposals.

1. Conduct a pre-implementation review

A pre-implementation review (PIR) can provide information an affected company needs to support smooth implementation of the requirements as they are finalized. It can also identify other improvements the company may want to make to existing processes, systems and controls and help the company prepare for CFPB examinations and other compliance reviews.

[1] Integrated Mortgage Disclosures NPR, Section V.A.

A PIR looks across the entirety of a company's mortgage-related processes and systems to identify the areas that will be affected. It could also include preliminary compliance risk assessments, leveraging existing risk assessments, to help the company focus on high-risk areas. In addition, a PIR can provide the company with the information it needs to comment on these and other NPRs or, as is discussed below, to issue a comment supporting the adoption of a reasonable implementation period.

A PIR can be useful at this stage of the rulemaking processes because, even without final rules, the statute and these proposals issued to date provide good indicators of expected final requirements. For example, an affected company can reasonably project much of the additional data and information the company will need to capture and manipulate (e.g., key loan terms and proposed data elements that will likely go into the computations of Annual Percentage Rate (APR), Transaction Coverage Rate (TCR), finance charges, etc.).

Similarly, a company can reasonably project that final rules are likely to require companies to make identifiable categories of process and system changes (and corresponding documentation changes) such as:

- Changing the timing of disclosures and collecting missing loan application information;
- Modifying record production, retention, and storage practices;
- Incorporating new disclosures and their respective triggers;
- Upgrading processes to meet servicing notices and standards; and
- Making changes to internal and external roles and responsibilities including handoffs, and making corresponding staffing adjustments.

Based on the results of the PIR, an affected company can develop its overall and specific implementation strategies, plan resources, and can begin advance work to the extent feasible. A company may also consider making business changes as an alternative approach to complying with various requirements. The company may also be able to obtain cost and time savings by integrating the expected change work into other existing or planned projects.

For the PIR and analysis to be most effective, the PIR should focus on integrating the changes into existing processes, systems, and business model to extent feasible. This may mean leveraging the strengths of existing processes and systems, and harmonizing the company's implementation with the company's strategies, operations, and culture. For example, a company may be able to harmonize compliance with consumer protection requirements with a customer-focused business strategy to make compliance less disruptive and more sustainable.

An affected company may also use the PIR and actions as a way to make process and systems improvements unrelated to compliance. For example, it may want to expand a compliance-driven automation project to better meet its core business needs at a relatively low additional cost. The company might also want to see how it could leverage its compliance efforts to find non-compliance-related efficiency gains or cost savings, or to better align processes and systems with the company's core strategies and objectives.

A PIR at this stage of the development of CFPB rules could also enable an affected company to prepare itself for future CFPB scrutiny by considering what its processes and systems might look like to the CFPB. The Bureau, as a new regulator, may be examining the company for the first time (and for nonbank mortgage companies it may be their first examination by any regulator). As the CFPB's Supervision and Examination Manual suggests, examiners typically form their impressions of examined company through their documents. A PIR can include review of the types of documentation that examiners will rely on, identify potential areas of increased regulatory risk and to develop approaches to mitigating that risk.

2. *Comment on a "reasonable implementation period" and other areas of concern*

In addition to taking steps to prepare for implementation of the impending Dodd-Frank mortgage provisions, an affected company concerned with implementation challenges may also want to comment on the Integrated Mortgage Disclosures NPR and any other areas of concern. The Integrated Mortgage Disclosure NPR indicates that the Bureau intends to:

- Issue a final rule prior to January 21, 2013 exempting affected companies from complying with the new Integrated Mortgage Disclosures until it issues a final regulation; and
- Include in its final rule a "reasonable implementation period."[2]

According to the CFPB's accompanying discussion, industry participants, including various lenders, mortgage brokers, settlement agents, forms vendors, and trade associations have asked the Bureau for an implementation period of at least 12 months.

The CFPB discussion does not comment on that request, favorably or unfavorably. Rather, the CFPB highlights its desire to make the rule effective as soon as possible, as well as its understanding that the final rule will require affected companies to revise their software and to retrain their staff and at the same time they will also be implementing other sets of Dodd-Frank mortgage-related provisions.

To balance those competing interests, the CFPB requests comments on how much time industry needs to make the changes necessary to implement the new disclosures, and specifically requests "details on the required updates and changes to systems and other measures that would be required to implement the rule and the amount of time needed to make those changes."[3]

The nature of this request is consistent with the Bureau's statutory mandate to use a fact-based data-driven model to evaluate the impact to institutions. Therefore, industry participants wanting the CFPB to adopt a 12-month or longer implementation period should consider submitting facts—singly, jointly or through trade associations—that would support such a period, including descriptions of the necessary process steps and the time required for each. As was mentioned above, a PIR could provide companies with the raw materials they would need to generate such a comment.

The NPR also specifically seeks comments on whether small and large entities should have different implementation periods. However, the Bureau also notes its concern that "a bifurcated implementation period could be detrimental to consumers."

In addition to commenting on the implementation period, affected companies also may want to comment on other aspects of the proposals, for example, whether proposed changes to the definition of "high cost loans," or related changes to the definition of "finance charge," would bring about unintended expansion of the range of loans that would fall into the high cost category; whether the timing of other aspects of the proposed disclosures would cause difficulties the CFPB may not have taken into account; or whether there are other issues that the company has been identified, for example, as a result of a PIR.

All comments related to the implementation period for the Integrated Mortgage Disclosures (and for comments on the proposed definitions of finance charge/APR for disclosure purposes and on the scope of certain exclusions from the application of the required disclosures) are due by September 7, 2012. All other comments on the Integrated Mortgage Disclosures proposal are due by November 7, 2012. All comments on the High-Cost Mortgage and Homeownership Counseling proposal are due by September 7, 2012.

---

[2] Id.

[3] Id.

Additional information

Primary authors:

Jeff Lavine	703 918 1379	jeff.lavine@us.pwc.com
Bruce Oliver	703 918 6990	bruce.oliver@us.pwc.com
Anthony Ricko	978 692 1701	anthony.ricko@us.pwc.com
Jason Ashenfelter	216 875 3153	jason.r.ashenfelter@us.pwc.com

For additional information about PwC's Financial Services Regulatory Practice and how we can help you, please contact:

Dan Ryan
Financial Services Regulatory Practice Chairman
646 471 8488
daniel.ryan@us.pwc.com

Alison Gilmore
Financial Services Regulatory Practice Marketing Leader
646 471 0588
alison.gilmore@us.pwc.com

www.pwcregulatory.com