



## LINKS

June 3, 2013

### FHA and Higher Priced Mortgage Loans

With the implementation of Mortgagee Letter 2013-04 on June 3, 2013, the monthly mortgage insurance premium on FHA loans with loan-to-value ratios exceeding 90% will apply for the life of the loan, rather than terminating when the loan amortizes to a 78% LTV. FHA recognizes that this change in policy will increase the annual percentage rate (APR) on FHA mortgages and may result in mortgages that exceed the higher priced mortgage loan standard outlined in Regulation Z.

Regulation Z defines a higher-priced mortgage loan (HPML) as a consumer credit transaction secured by the consumer's 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 loans secured by a first lien, or by 3.5 or more percentage points for loans secured by a subordinate lien. (The escrow account requirements also employ a separate threshold of 2.5 percentage points over APOR for "jumbo" mortgages, but this is not relevant for FHA loans.)

To the extent lenders are concerned about the status of FHA's rulemaking with respect to the Dodd-Frank ability to repay standard and FHA's qualified mortgage standards, FHA is working to define an FHA QM standard that meets the Dodd-Frank purposes, takes HPMLs into account, and addresses the needs of the marketplace for lender and investor certainty. FHA looks forward to the active engagement of all interested parties in achieving a timely and thoughtful approach to these complex issues.

In the near term, FHA understands that mortgages exceeding the HPML threshold will also have to comply with the existing requirements for such loans under Regulation Z. This is currently true for FHA loans that exceed the HPML threshold, but we understand that implementation of ML 2013-04 may cause additional loans to exceed this threshold. We have heard that some lenders have concerns about these existing requirements and,

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in an effort to address those concerns, have consulted with the Consumer Financial Protection Bureau (CFPB) on the following guidance related to escrow accounts, appraisals, ability to repay and prepayment penalties. FHA expects lenders to fully comply with all applicable requirements for loan origination, including requirements that are established under Regulation Z for HPMLs. We have outlined below where HPML requirements would differ from FHA requirements:

1. **Escrow Accounts:** Regulation Z requires an escrow account for all first-lien HPMLs. Escrow accounts are also required on all FHA loans. Although the HPML rules generally permit (but do not require) cancellation of mandatory escrow accounts after five years and upon the consumer's request, FHA does not permit cancellation of required escrow accounts at any time, thus lenders may not cancel escrow accounts on FHA loans whether they are HPMLs or not.
2. **Appraisals:** The existing Regulation Z does not contain specific appraisal requirements and lenders are expected to continue complying with FHA's appraisal requirements. Commencing January 18, 2014, Regulation Z's appraisal requirements will require a full, interior-inspection appraisal for HPMLs with some exceptions. One such exception is for QMs.
3. **Ability to Repay:** The CFPB has outlined its ability-to-repay requirements in its final rule that will take effect January 10, 2014. In the interim period before those requirements become effective, the repayment ability requirement previously established by the Federal Reserve Board at 12 CFR 1026.35(b)(1), which will move to section 1026.35(e)(1) as of June 1, 2013, continues to apply. FHA has consulted with the CFPB and believes that its requirements, found in the current 4155.1, are sufficient to satisfy the Regulation Z ability-to-repay requirements for those FHA-insured loans that will be HPMLs, with certain exceptions: Streamline Refinances and ARMs may not satisfy the existing, HPML ability-to-repay requirements, depending on how they are underwritten. For example, Streamline Refinances that are HPMLs, and where income or assets relied on are not verified by obtaining confirming documentation, do not meet the ability-to-repay requirements. For these exceptions, lenders must go beyond the applicable FHA requirements to comply with the HPML ability-to-repay requirements.

4. **Prepayment Penalties:** CFPB has determined that monthly interest accrual amortization, which FHA permits, should be considered a prepayment penalty. However, recognizing that HUD must engage in rulemaking to end this practice, CFPB has stated in its final rule published on January 30, 2013, that monthly interest accrual amortization is not a prepayment penalty for FHA loans consummated before January 21, 2015.

