TILA Section 35 (HPML) Breakdown

From: Compliance Team

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Subject: TILA Section 35 (HPML) Breakdown

General:

This TILA section applies to a closed-end mortgage loan secured by the consumer's principal dwelling wherein the APR exceeds APOR by more than the allowed margin, which varies depending on loan type. APOR is based on the date the interest rate is set.

Escrow Account Requirements:

An escrow account need not be established for transactions secured by shares in a cooperative, financing initial construction of a dwelling (although the perm phase of a one-time close is still subject to HPML requirements), a temporary or bridge loan of 12 months or less in term, or a reverse mortgage.

There is an additional exemption for small creditors that meet the Rural and Underserved Area creditor guidelines. The details of this exemption can be found here:
https://www.bankersonline.com/reg ulations/12-1026- 035# b2iii

If an escrow account is established due to HPML requirements, the escrow account may not be cancelled until either the debt obligation is terminated (paid in full, refinanced, etc.) or the borrower makes the request at least 5 years after consummation and the unpaid principal balance is less than 80% of the original property value, and the loan is not delinquent or in default.

Appraisal Requirements:

If the loan is an HPML, a written appraisal performed by a certified or licensed appraiser who conducts a physical visit of the interior of the collateral property is required.

Two written appraisals are required to be performed by different certified or licensed appraisers on a purchase transaction if the collateral property was acquired by the seller 90 days or fewer prior to the buyer's agreement to acquire the property and the sales price exceeds the seller's acquisition price by more than 10%, or the collateral property was acquired by the seller 91 to 180 days prior to the buyer's agreement to acquire the property and the sales price exceeds the seller's acquisition price by more than 20%.

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An appraisal is not required in the following instances:

- The loan is a qualified mortgage
- The loan amount is equal or less than the applicable threshold amount ($33,500 for 2025)
- The transaction is secured by a mobile home, boat, or trailer
- The transaction is to finance the initial construction of a dwelling
- A loan term of 12 months or less
- A reverse mortgage transaction
- An extension of credit that is a refinancing secured by a first lien, with refinancing defined as in § 1026.20(a) (except that the creditor need not be the original creditor or a holder or servicer of the original obligation), provided that the refinancing meets the following criteria:

(A) Either—

(*1*) The credit risk of the refinancing is retained by the person that held the credit risk of the existing obligation and there is no commitment, at consummation, to transfer the credit risk to another person; or
(*2*) The refinancing is insured or guaranteed by the same Federal government agency that insured or guaranteed the existing obligation;

(B) The regular periodic payments under the refinance loan do not

(*1*) Cause the principal balance to increase;
(*2*) Allow the consumer to defer repayment of principal; or
(*3*) Result in a balloon payment, as defined in § 1026.18(s)(5)(i); and

(C) The proceeds from the refinancing are used solely to satisfy the existing obligation and amounts attributed solely to the costs of the refinancing.

- A transaction secured by:

(A) A new manufactured home and land, but the exemption shall only apply to the requirement that the appraiser conduct a physical visit of the interior of the new manufactured home; or

(B) A manufactured home and not land, for which the creditor obtains one of the following and provides a copy to the consumer no later than three business days prior to consummation of the transaction—

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(*1*) For a new manufactured home, the manufacturer's invoice for the manufactured home securing the transaction, provided that the date of manufacture is no earlier than 18 months prior to the creditor's receipt of the consumer's application for credit;
(*2*) A cost estimate of the value of the manufactured home securing the transaction obtained from an independent cost service provider; or
(*3*) A valuation, as defined in § 1026.42(b)(3), of the manufactured home performed by a person who has no direct or indirect interest, financial or otherwise, in the property or transaction for which the valuation is performed and has training in valuing manufactured homes.

Thresholds:

A mortgage transaction is considered an HPML if the APR exceeds APOR by:

- 1st lien – 1.5% or more if the principal loan amount does not exceed the FNMA conforming loan limit
- 1st lien – 2.5% or more if the principal loan amount exceeds the FNMA conforming loan limit
- Subordinate lien – 3.5% or more

Requirements:

Failing the Section 35 test leads to additional escrow and appraisal requirements. Unless otherwise exempt, creditor must establish an escrow account prior to loan consummation for the first 5 years of the transaction.

Resources:

Reg. Z § 1026.35: https://www.bankersonline.com/regulations/12- 1026- 035

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