adjustment to the escrows exemption asset-size threshold will also decrease the threshold for small-creditor portfolio and balloon-payment qualified mortgages under Regulation Z. The requirements for small-creditor portfolio qualified mortgages at § 1026.43(e)(5)(i)(D) reference the asset threshold in § 1026.35(b)(2)(iii)(C). Likewise, the requirements for balloon-payment qualified mortgages at § 1026.43(f)(1)(vi) reference the asset threshold in § 1026.35(b)(2)(iii)(C). Balloon-payment qualified mortgages that satisfy all applicable criteria in §§ 1026.43(f)(1)(i) through (vi) and 1026.43(f)(2), or the conditions set forth in § 1026.32(d)(1)(i)(C), are also excepted from the prohibition on balloon payments for high-cost mortgages in § 1026.32(d)(1)(i)(C).

II. Procedural Requirements
A. Administrative Procedure Act
Under the Administrative Procedure Act (APA), notice and opportunity for public comment are not required if the Bureau finds that notice and public comment are impracticable, unnecessary, or contrary to the public interest. 5 U.S.C. 553(b)(B). Pursuant to this final rule, comment 35(b)(2)(iii)–1 in Regulation Z is amended to update the exemption threshold. The amendment in this final rule is technical, and merely applies the formula previously established in Regulation Z for determining any adjustments to the exemption threshold. For these reasons, the Bureau has determined that publishing a notice of proposed rulemaking and providing opportunity for public comment are unnecessary. Therefore, the amendment is adopted in final form.

Section 553(d) of the APA generally requires publication of a final rule not less than 30 days before its effective date, except for (1) a substantive rule which grants or recognizes an exemption or relieves a restriction; (2) interpretive rules and statements of policy; or (3) as otherwise provided by the agency for good cause found and published with the rule. 5 U.S.C. 553(d). At a minimum, the Bureau believes the amendments fall under the third exception to section 553(d). The Bureau finds that there is good cause to make the amendments effective on January 1, 2016. The amendment in this rule is technical, and applies the method previously established in the agency’s regulations for automatic adjustments to the threshold.

B. Regulatory Flexibility Act
Because no notice of proposed rulemaking is required, the Regulatory Flexibility Act does not require an initial or final regulatory flexibility analysis. 5 U.S.C. 603(a), 604(a).

C. Paperwork Reduction Act
In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3506; 5 CFR 1320), the agency reviewed this final rule. No collections of information pursuant to the Paperwork Reduction Act are contained in the final rule.

List of Subjects in 12 CFR Part 1026
Advertising, Consumer protection, Credit, Credit unions, Mortgages, National banks, Reporting and recordkeeping requirements, Savings associations, Truth in lending.

Authority and Issuance
For the reasons set forth in the preamble, the Bureau amends Regulation Z, 12 CFR part 1026, as set forth below:

PART 1026—TRUTH IN LENDING (REGULATION Z)

1. The authority citation for part 1026 continues to read as follows:


2. In Supplement I to Part 1026—Official Interpretations, under Section 1026.35—Requirements for Higher-Priced Mortgage Loans, 35(b)(2) Exemptions, Paragraph 35(b)(2)(iii), paragraph 1.i.i.E introductory text, as amended at 80 FR 59968 (Oct. 2, 2015), is revised to read as follows:

SUPPLEMENT I TO PART 1026—OFFICIAL INTERPRETATIONS

Subpart E—Special Rules for Certain Home Mortgage Transactions

Section 1026.35—Requirements for Higher-Priced Mortgage Loans

35(b)(2) Exemptions

Richard Cordray,
Director, Bureau of Consumer Financial Protection.

[FR Doc. 2015–32293 Filed 12–22–15; 8:45 am]

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FEDERAL HOUSING FINANCE AGENCY

12 CFR Part 1227

RIN 2590–AA60

Suspected Counterparty Program

AGENCY: Federal Housing Finance Agency.

ACTION: Final rule.

SUMMARY: This final rule establishes requirements and procedures for the Federal Housing Finance Agency’s (FHFA) Suspected Counterparty Program. Under the Suspected Counterparty Program, FHFA may issue suspension orders directing the regulated entities (Fannie Mae, Freddie Mac, and the eleven Federal Home Loan Banks (Banks)) to cease doing business with an individual or institution, and any affiliate thereof, for a specified period of time where such party has committed fraud or other financial misconduct involving a mortgage transaction.

The final rule revises the interim final rule published on October 23, 2013. The final rule excludes from the types of covered transactions that would be subject to a final suspension order any transaction involving a residential mortgage loan if the loan is secured by the respondent’s own personal or

4 The Bureau extended the temporary provision in § 1026.43(e)(6) from covered transactions consummated on or before January 10, 2016 to covered transactions for which the application was received on or before April 1, 2016. See 80 FR 59943, 59959 (Oct. 2, 2015).
household residence. The final rule provides more time than the interim final rule published on October 23, 2013. 78 FR 63007. FHFA received two comment letters on the interim final rule: one from Fannie Mae; and one from eleven of the then twelve Banks 1 (the Pittsburgh Bank did not join in the comment letter). The current regulation, the comments received, and the final rule are discussed below.

II. Analysis of Final Rule

A. Requirement to Submit Reports—§ 1227.4

1. Scope of Reporting Requirements

Current regulation. The current regulation requires a regulated entity to submit a report to FHFA when the regulated entity becomes aware that a person or affiliate thereof with which the regulated entity is engaging or has engaged in a covered transaction within the past three years has engaged in covered misconduct. A regulated entity is aware of covered misconduct when the regulated entity has reliable information that such misconduct has occurred. 12 CFR 1227.4(a). “Covered misconduct” is defined to include convictions or administrative sanctions based on fraud or similar misconduct in connection with the mortgage business. 12 CFR 1227.2. The Federal Register notice accompanying the interim final rule states that the regulated entities are not required to conduct any independent investigation of the underlying conduct. See 78 FR at 63009.

Comments received. The Banks supported the requirement in the current regulation for reporting to FHFA when “they become aware” of covered misconduct based on “reliable information.” The Banks also asked that FHFA provide additional guidance on the scope of their reporting obligations with respect to “reliable information.” The Banks recommended that the rule language indicate that the regulated entities are not required to conduct any independent investigation of the conduct underlying covered misconduct. The Banks also asked that the rule language indicate that the regulated entities would not be required to conduct any docket searches for convictions or to monitor federal agency notices of debarment. The Banks also recommended that the reporting requirements not apply where a regulated entity becomes aware of covered misconduct through national news reporting or by an announcement or action taken by a federal agency, stating that such information would be accessible to FHFA as well as the regulated entities and all regulated entities should not have to report on the same, widely known conduct. The Banks further recommended that the reporting requirements not apply to any information about covered misconduct that a regulated entity discovers in reviewing a member’s examination report. The Banks stated that their review of such reports is subject to confidentiality agreements with federal financial regulators that limit their ability to disclose any information in the reports without the express written consent of the regulator.

Final rule. The final rule does not change the scope of the reporting requirements under the Suspended Counterparty Program. A regulated entity is required to submit a report to FHFA regarding only covered misconduct of which the regulated entity is aware. The extent of any regulated entity’s efforts in evaluating counterparties or addressing potential mortgage fraud is a prudential matter for the regulated entity, subject to regular supervision by FHFA. The Suspended Counterparty Program is not intended to require additional review or investigation by a regulated entity, nor is it intended to take the place of any review or investigation that a regulated entity would otherwise engage in.

With respect to the comment regarding confidential examination information, the Suspended Counterparty Program is limited to convictions or administrative sanctions for fraud or other financial misconduct related to mortgage transactions. Records regarding any such actions would be publicly available, so it would not be necessary to revise this rule to address confidential examination information.

2. Scope of Screening

Current regulation. The Federal Register notice accompanying the interim final rule states that the rule does not specify the internal procedures that each regulated entity must establish to ensure compliance with the reporting requirements under the rule. See 78 FR at 63009.

Comments received. The Banks indicated that they have existing procedures for screening against the U.S. Treasury Department’s Office of Foreign Assets Control’s list. The Banks requested that FHFA state that such...
procedures are sufficient for purposes of the Suspended Counterparty Program. Fannie Mae commented that screening individual purchasers of Fannie Mae-owned real estate (REO) against the FHFA suspended counterparty list would present operational challenges. Fannie Mae requested FHFA to state that such screening is not required.

Final rule. The Suspended Counterparty Program is not intended to define the scope of a regulated entity’s internal procedures to address risks presented by fraud or other financial misconduct. Each regulated entity must establish appropriate procedures to address such risks. The Suspended Counterparty Program supplements the efforts of the regulated entities; it does not replace those efforts. For example, the Suspended Counterparty Program does not by itself require a regulated entity to screen individual REO purchasers against the FHFA suspended counterparty list, but a regulated entity may still do so if the regulated entity determines that such screening would be a prudent business practice.

3. Timing of Reports

Current regulation. The current regulation defines “covered transaction” to include a transaction involving persons or institutions with whom Fannie Mae no longer does business even if they have already ceased doing business with a particular individual or institution. Fannie Mae commented that ten business days is not sufficient to complete necessary diligence and reasonable investigation to confirm whether there is in fact covered misconduct and whether or not Fannie Mae is engaged in a covered transaction with the reported party. Fannie Mae noted that such investigations typically rely on public information that may not be available within such timeframe. Fannie Mae asked FHFA to extend the time for submitting reports to 30 calendar days.

Final rule. FHFA recognizes that in some instances ten business days may not be sufficient to complete necessary investigation or other due diligence. Accordingly, the final rule revises the time for submitting reports to 30 calendar days.

B. Timing Requirements for Covered Transactions—§§ 1227.4, 1227.5 and 1227.6

Current regulation. The Suspended Counterparty Program covers situations where an individual or institution has engaged in a covered transaction with a regulated entity within the past three years. The current regulation requires a regulated entity to report to FHFA when it becomes aware that a person or affiliate thereof with which the regulated entity is engaging or has engaged in a covered transaction within the past three years has engaged in covered misconduct. 12 CFR 1227.4(a).

The current regulation also provides that a proposed or final order of suspension may be issued if the suspending official determines that there is evidence that the regulated entity engaged in a covered transaction with the person or affiliate thereof within the past three years and has engaged in covered misconduct. 12 CFR 1227.5(b)(1) and 1227.6(a)(1).

Comments received. Both Fannie Mae and the Banks asked that the rule be limited to current counterparties, not counterparties with which they have done business within the past three years. The Banks indicated that their current procedures for identifying covered misconduct under the Suspended Counterparty Program do not address persons that have ceased doing business with the Banks and stated that requiring reports on such persons would be unduly burdensome. Fannie Mae commented that requiring reports on covered misconduct involving persons or institutions with whom Fannie Mae no longer does business would be an inefficient use of resources. Fannie Mae noted that requiring a regulated entity to research whether a contract or agreement terminated two or three or four years ago would yield very little benefit and would not fulfill the purposes of the Suspended Counterparty Program.

Final rule. The final rule revises the standard for issuing a proposed or final suspension order to eliminate the requirement that FHFA demonstrate that the regulated entity has done business with the individual or institution within the past three years. However, the final rule maintains the requirement that a regulated entity submit reports regarding any parties with which it has done business within the past three years. FHFA recognizes that it may be difficult for a regulated entity to determine the exact date it ceased doing business with a particular individual or institution. In addition, documenting the exact timing of the most recent covered transaction is not necessary to accomplish the purposes of the Suspended Counterparty Program. Suspension orders reflect a determination by FHFA that doing business with an individual or institution presents a safety and soundness risk to the regulated entities. This determination is forward-looking and does not depend on whether a regulated entity has recently engaged in a covered transaction. For those reasons, the final rule eliminates the requirements in §§ 1227.5(b)(1) and 1227.6(a)(1) that FHFA demonstrate that a regulated entity has done business with the individual or institution within the past three years.

Although the final rule revises the standard for whether FHFA may issue a proposed or final suspension order, the final rule maintains the requirement in § 1227.4(a) that the regulated entities submit reports in appropriate cases, even if they have already ceased doing business with the individual or institution. In many cases, a regulated entity may take action to terminate its relationship with a party before there has been any conviction or administrative sanction that would trigger the reporting requirement under the Suspended Counterparty Program. In some cases, a regulated entity may have stopped doing business with a counterparty that is currently doing business with another regulated entity that is not yet aware of the covered misconduct. Therefore, excluding those cases from the coverage of the rule would undermine the effectiveness of the program.

To the extent records are available, the regulated entities are encouraged to submit reports on any individual or institution that has engaged in covered misconduct regardless of when the most recent covered transaction took place. However, recognizing the practical and operational difficulty of determining when the most recent transaction may have occurred, the final rule only requires a regulated entity to submit reports regarding any parties with which it has done business within the past three years.

C. Definitions—§ 1227.2

1. Covered Transaction

Current regulation. The current regulation defines “covered transaction” as “a contract, agreement, or financial or business relationship between a regulated entity and a person and any affiliates thereof.” 12 CFR 1227.2. The Federal Register notice accompanying the interim final rule invited comments on whether this definition should be revised to include more explicit standards. As an example, the notice asked whether the rule should cover “lower tier covered transactions” to address persons who may indirectly do business with a regulated entity, such as a subcontractor or other person providing services to a party that does
business directly with a regulated entity. See 78 FR at 63009.

Comments received. The Banks commented that the regulation should not cover lower tier covered transactions. The Banks indicated that it would not be possible in all cases to require their counterparties to ensure that the counterparties did not do business with any suspended party in connection with a covered transaction and that the Banks would be unable to effectively monitor such a requirement in cases where a counterparty did agree to the requirement. The Banks commented that it would be possible for the Banks to encourage their counterparties not to do business with entities that have been suspended by FHFA.

Fannie Mae commented that the regulated entities should not be required to directly ensure that a suspended party does not do business indirectly with a regulated entity. Fannie Mae indicated that it would be operationally difficult for Fannie Mae to attempt to monitor such relationships between third parties. Fannie Mae commented that it could notify its counterparties of any limitations imposed by FHFA on such transactions, but it would not be able to directly ensure compliance.

Fannie Mae also recommended that the definition of “covered transaction” be limited to “contract or agreement” and not include other “financial or business relationships.” Fannie Mae stated that “financial or business relationships” is redundant with “contract or agreement,” and that if it was intended to capture something beyond a contract or agreement, it is too broad and ambiguous. Fannie Mae expressed concern that “financial or business relationships” could be interpreted to include relationships with service providers such as delivery services for which Fannie Mae may have an account but not necessarily a contract or agreement, which it stated would not advance the purposes of the Suspended Counterparty Program.

Final rule. The final rule does not revise the definition of “covered transaction.” In many cases involving mortgage fraud, a regulated entity that has purchased a mortgage loan may be directly affected by the fraud despite the fact that none of the parties that engaged in fraudulent conduct has a direct relationship with the regulated entity. However, FHFA recognizes that it would be operationally difficult at this time for the regulated entities to effectively monitor relationships between their counterparties and such lower tier service providers. For that reason, FHFA is not at this time requiring that the regulated entities report on transactions between their direct counterparties and lower tier parties, or that the regulated entities ensure that their direct counterparties cease doing business with any lower tier parties that have been suspended by FHFA.

FHFA expects the regulated entities to take all appropriate measures to address the risks presented by mortgage fraud. The scope of those measures may depend in part on the nature of the financial or business relationship between the party and the regulated entity. Limiting the definition of “covered transaction” to only a “contract or agreement,” as recommended by Fannie Mae, would be too restrictive and, thus, contrary to the intent of the Suspended Counterparty Program. FHFA intends the definition to be flexible enough to encompass any parties who present a particular risk to the regulated entities, while still excluding generic third party service providers that are only incidentally involved in mortgage-related transactions, such as mail and package delivery vendors.

While the final rule does not limit the general definition of “covered transaction” in response to the comments received, the final rule limits the scope of a final suspension order to exclude one category of what otherwise might be considered lower tier covered transactions. FHFA does not intend final suspension orders to prevent respondents or their households from obtaining mortgage financing for the respondent’s own personal or household residence. The final rule adds a new paragraph (d) to § 1227.3 making clear that final suspension orders do not have any effect on any transaction involving a residential mortgage loan if the loan is secured by the respondent’s own personal or household residence.

2. Affiliate

Current regulation. The current regulation defines “affiliate” as a party that controls or is controlled by another person, whether directly or indirectly, including situations where one or more persons are controlled by the same third person. 12 CFR 1227.2.

Comments received. The Banks supported defining “covered misconduct” as limited to offenses in connection with the mortgage business. The Banks suggested restating the definition of “covered misconduct” as certain types of conduct resulting in conviction or administrative sanction rather than a conviction or administrative sanction based on certain types of conduct. The Banks suggested that this would make clear that the conduct being imputed is the conduct that gave rise to the conviction or administrative sanction and not the conviction or administrative sanction itself.

Final rule. The final rule does not change the definition of “covered misconduct.” FHFA does not engage in independent fact-finding regarding the conduct underlying a conviction or administrative sanction covered by the rule. The current regulation reflects this approach by defining “covered misconduct” explicitly in terms of convictions and administrative sanctions. Where FHFA proceeds with a proposed or final suspension with respect to an affiliate, FHFA is imputing not just the underlying conduct, but the “covered misconduct” as defined in the rule.
4. Administrative Sanctions

Current regulation. The current regulation defines “administrative sanction” as a debarment, suspension, or any similar administrative sanction imposed by a Federal agency that has the effect of limiting the ability of a person to do business with a Federal agency. 12 CFR 1227.2. The definition includes any settlements of a proposed administrative sanction if the settlement has the same effect. The Federal Register notice accompanying the interim final rule requested comment on whether the definition should include other types of administrative sanctions, such as enforcement actions by other financial institution regulators. See 78 FR at 63009.

Comments received. Fannie Mae commented that the definition in the current regulation is appropriate and sufficiently broad and, therefore, should not be expanded to include enforcement actions by other financial institution regulators.

Final rule. The final rule does not change the definition of “administrative sanction” to include other types of administrative sanctions, such as enforcement actions by other financial regulators. The Suspended Counterparty Program is a limited measure intended to reduce the risks to the regulated entities from fraud and other financial misconduct. Other kinds of administrative actions may or may not be related to the goals of the Suspended Counterparty Program. FHFA may consider expanding the definition of “administrative sanction” in the future, but only in appropriate circumstances related to the goals of the Suspended Counterparty Program.

5. Conviction

Current regulation. The current regulation defines “conviction” as any judgment or other determination of guilt of a criminal offense by a court of competent jurisdiction, or any other functionally equivalent resolution. 12 CFR 1227.2. The definition includes judgments entered by verdict or based on a guilty plea. Other dispositions, such as probation before judgment or deferred prosecution, are also included if they include an admission of guilt.

Comments received. The Banks asked that FHFA state that “a court of competent jurisdiction” is limited to courts of the United States of America and does not include courts in foreign jurisdictions.

Final rule. The final rule does not change the definition of “conviction.” FHFA intends the definition of conviction to encompass both state and federal courts. FHFA has not received any reports to date based on a conviction from a court outside the United States. If FHFA receives any such report in the future, FHFA will further evaluate the report to determine whether any additional action is necessary or appropriate.

D. Written Notice of Proposed Suspension

Current regulation. The current regulation provides that if the suspending official determines that there are grounds for a proposed suspension order, the suspending official “may” issue a written notice of proposed suspension. 12 CFR 1227.5(c).

Comments received. The Banks commented that a written notice of proposed suspension is necessary to enable affected parties to respond. The Banks, therefore, recommended that issuance of a written suspension notice should be mandatory where a suspending official finds grounds for such issuance.

Final rule. The final rule does not change this provision of the regulation. The use of the permissive “may” rather than the mandatory “shall” in this sentence is appropriate because the decision to propose suspension is a discretionary decision by FHFA. For example, the suspending official may determine that there are grounds for a proposed suspension order but that for other reasons a proposed suspension is not appropriate. The existing provision correctly expresses the discretionary nature of the decision to propose suspension. If the suspending official decides that a written notice of proposed suspension should be issued to the affected person, the suspending official must provide notice of the proposed suspension to each of the regulated entities as well.

While the final rule does not change the substance of this provision, the final rule clarifies the method of sending a notice of proposed suspension. Under the final rule, a notice of proposed suspension will be sent to an affiliate of a respondent only if the affiliate would be subject to the proposed suspension. The final rule also makes technical drafting changes to the language on the method of sending notices for greater clarity.

E. Scope of Final Suspension Orders

Current regulation. The current regulation provides that a final suspension order may be issued directing the regulated entities to cease or refrain from engaging in covered transactions “with a particular person and any affiliates thereof.” 12 CFR 1227.3(a).

Comments received. The Banks commented that this language should be revised to clarify that each suspended affiliate will be identified in the suspension order. The Banks noted that it is difficult, if not impossible, for the regulated entities to know the full extent of the affiliates of any given entity.

Final rule. The final rule does not change this provision of the regulation. Section 1227.9(f)(2)(ii) states that each final suspension order must identify “each person and any affiliates thereof to which the suspension applies.” It is not necessary to restate this requirement in §1227.3(a).

F. Status of Previous FHFA Guidance

Comments received. The Banks requested that, in order to eliminate potential conflicts of interpretation, FHFA state that any FHFA guidance issued prior to the interim final rule has been superseded by the interim final rule. The Banks also asked whether existing FHFA reporting forms should continue to be used for submitting reports.

Final rule. The Suspended Counterparty Program was established in June 2012 by letter to the regulated entities. Prior to publication of the interim final rule on October 23, 2013, FHFA adopted procedures for the regulated entities to submit reports and provided informal guidance on the scope of the reporting obligations. While the interim final rule generally codified the existing procedures for the Suspended Counterparty Program, to avoid unnecessary confusion, FHFA views any guidance issued prior to the effective date of the interim final rule as superseded. FHFA may respond to questions from the regulated entities about implementation and interpretation of the final rule, and FHFA may provide written guidance on specific issues as appropriate.

III. Consideration of Differences Between the Banks and the Enterprises

Section 1313(f) of the Federal Housing Enterprises Financial Safety and Soundness Act requires FHFA, when promulgating regulations relating to the Banks, to consider the differences between Fannie Mae and Freddie Mac (collectively, the Enterprises) and the Banks with respect to the Banks': cooperative ownership structure; mission of providing liquidity to members; affordable housing and community development mission; capital structure; and several liability; and any other differences FHFA considers appropriate. See 12 CFR 1227.3(a).
§ 1227.3 Scope of suspension orders.  
* * * * *  
(d) No effect on residential mortgage loans secured by respondent’s own personal or household residence. A final suspension order issued pursuant to this part shall have no effect on any transaction involving a residential mortgage loan if the loan is secured by the respondent’s own personal or household residence.  

§ 1227.4 [Amended]  
3. Amend § 1227.4(c)(1) by removing the phrase “ten (10) business days” and adding in its place the phrase “thirty (30) calendar days”.  

§ 1227.5 [Amended]  
4. Amend § 1227.5 by  
   a. Removing the phrase “regulated entity is engaging or engaged in a covered transaction with the person or any affiliates thereof within the past three (3) years and the” from paragraph (b)(1).  
   b. Revising paragraph (e) to read as follows:  

§ 1227.5 Proposed suspension order.  
* * * * *  
(e) Method of sending notice. The suspending official shall send the notice of proposed suspension to the last known street address, facsimile number, or email address of:  
   (1) The person, the person’s counsel, or an agent for service of process; and  
   (2) Any affiliates of the person, the counsel for those affiliates, or an agent for service of process, if suspension is also being proposed for such affiliates.  
* * * * *  

§ 1227.6 [Amended]  
5. Amend § 1227.6(a)(1) by removing the phrase “regulated entity is engaging or has engaged in a covered transaction within the past three (3) years with the respondent, and the”.


Melvin L. Watt,  
Director, Federal Housing Finance Agency.

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