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QM, QRM, and the Ability to Repay Rule

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The Rule

- No creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination based on verified and documented information that, at the time the loan is consummated, the consumer has a reasonable ability to repay the loan, according to its terms, and all applicable taxes, insurance (including mortgage guarantee insurance), and assessments

- Effective Date – January 10, 2014

Potential Damages

$300,000 @ 4.6%

Origination Fee 2%	$ 6,000
3yr. Finance Charge	$40,000
Actual Damages (down payment)	$30,000
Attorney Fees (plaintiff)	$50,000
Total Damages	$126,000

- Chief Economist for Mortgage Bankers Association: costs of a successful lawsuit against a lender would likely be $180,000 – $200,000

Coverage of the Ability to Repay Rule (ATR)

- Any consumer credit transaction that is secured by a 1- to 4-family dwelling, including any real property attached to a dwelling (covered transaction), other than
  - Home equity lines of credit
  - Timeshares
  - Reverse mortgages
  - Temporary or “bridge” loans with terms of 12 months or less, such as loans to finance the purchase of a new dwelling where the consumer plans to sell a current dwelling within 12 months or loans to finance the initial construction of a dwelling
  - The construction phase of 12 months or less of a construction-to-permanent loan

ATR Minimum Underwriting Requirements

- Creditors must, at a minimum, consider and verify, in most cases using reasonably reliable third party records, at least the following 8 underwriting factors:
  - Current or reasonably expected income or assets;
  - Current employment status;
  - Monthly payment on the covered transaction;
  - Monthly payment on any simultaneous loan;
  - Monthly payment for mortgage-related obligations;
  - Current debt obligations;
  - Monthly debt-to-income ratio or residual income; and
  - Credit history
- Special rules for verifying income and assets for ARM loans, balloon payments, interest-only loans, and negative amortization loans.
- Exemption for community housing lenders and certain non-profits

Qualified Mortgage (QM) Safe Harbor

- Safe Harbor is generally available for creditors and assignees if the loan is a QM
- Four types:
  - General QM
  - Special Rule QM
  - Qualified Mortgage Balloon Loans
  - Small Creditor Portfolio QM

General QM

- The lender has considered and verified the borrower's ATR
- The loan does not have certain features:
  - interest-only
  - negative amortization
  - balloon (i.e., a loan with a term of less than five years, and with regular periodic payments that do not fully amortize the outstanding principal balance)
- Term ≤ 30 years
- Total points and fees ≤ 3% (special rule for loans < $100,000)
- Debt-to-income ratio does not exceed 43%
- Safe Harbor is available for loans that are not "higher-priced" – i.e., <1.5% above the average prime offer rate (APOR) for first-lien loans and <3.5% above the APOR for subordinate lien loans – otherwise a rebuttable "presumption of compliance" for higher priced loans

Special Rule QM

- A temporary special category of QM
- A loan is a qualified mortgage if it meets the statutory limitations on product features, term, and points and fees and is eligible for purchase, guarantee, or insurance by
  - Fannie Mae or Freddie Mac while they are under conservatorship
  - FHA, VA, USDA
  - USDA Rural Housing Service
- With respect to GSE-eligible loans, this temporary provision expires when conservatorship of the GSEs ends
- With respect to each other category of loan, this provision expires either when the agency issues its own QM rule and, in any event, no later than January 10, 2021

Qualified Mortgage Balloon Loans

- A limited exception for smaller lenders that operate predominantly in rural or underserved areas
- Loan must satisfy the applicable limitations on product features and points and fees and must generally comply with ATR requirements
- Creditor's total assets ≤ $2 billion
- Creditor and affiliates together originated no more than 500 first-lien covered transactions in the preceding calendar year
- More than 50% of the creditor's first-lien covered transactions must be secured by properties in counties that are ''rural'' or ''underserved''
- The loan must generally be kept in portfolio for 3 years, with some exceptions

Small Creditor Portfolio QM

- Amendment to ATR/QM Rule to facilitate lending by community banks and credit unions, regardless of whether they operate in rural or underserved areas
- Loan must satisfy the statutory limits on product features and points and fees and generally must comply with the ATR requirements
- Creditor’s total assets ≤ $2 billion
- Creditor and affiliates together originated no more than 500 first-lien transactions in the preceding calendar year
- QM status to loans held in portfolio even if DTI > 43%
- Balloon Loans – two-year transition period for small lenders not in rural or underserved areas to make balloon loans while CFPB studies the issue
- Small creditors may charge up to 3.5% above APOR for first-lien QMs and still maintain the safe harbor

The Revised QRM Proposal

- Dodd Frank Section 941 requires retention of at least 5% of the credit risk of assets that collateralize asset-backed securities – exempts securitizations that consist exclusively of Qualified Residential Mortgages
- Federal Agencies (FDIC, FRB, OCC, SEC, FHFA and HUD) release long-awaited rewrite of its QRM proposal on 8/28/2013
- Definition of QRM=QM under CFPB QM/Ability to Repay Rule
- Downpayment requirement eliminated
- Agencies invited for comment an alternative the “QM-plus”