LAW OFFICES OF
MORTON W. BAIRD II

<u>Ability-to-Repay and Qualified Mortgage Rule (ATR/QM Rule)- Effective 1/10/14</u>

1) Dodd Frank requires that lenders make a reasonable, good-faith determination that the loan applicant has a reasonable ability to repay the loan under its terms.

2) The ATR/QM Rule applies to almost all closed end consumer credit transactions secured by a dwelling. This means loans made to consumers and secured by residential structures that contain 1-4 units, including condominiums.

3) The ATR/QM Rule does not apply to HELOCs, loans secured by vacant land, or loan modifications. It would apply to refinances.

4) Lender must consider a minimum of eight underwriting factors:

    i. Current or reasonably expected income or assets that the consumer will rely on to repay the loan

    ii. Current employment status

    iii. Monthly mortgage payment for the loan using the fully-indexed rate that will amortize the loan

    iv. Monthly payments on any simultaneous loans on the property

v. Monthly payments for property taxes and insurance

vi. Debts, alimony, child support obligations

vii. Monthly debt-to-income ratio or residual income

viii. Credit History

5) Note: Lenders should check to ensure that their underwriting policies and procedures reflect each of the eight factors.

6) Lender must verify information relied upon using reasonably reliable third-party records. Lender cannot rely on what the applicant tells them about their income.

7) Appendix Q to Regulation Z provides some flexibility in verifying information:

   i. In addition to W-2 or payroll statements, lenders can verify income using tax returns, bank statements, receipts from check-cashing, benefits program documentation, or records from an employer.

   ii. Employment status can be documented by calling the employer and getting oral verification, as long as a record of the call is kept.

   iii. Credit reports can be used to verify debt obligations.

   iv. If the applicant does not have a credit history from a credit bureau, the lender can verify credit history using documents that show nontraditional credit references, such as rental payment history or utility payments.

8) Dodd-Frank created a new consumer cause of action against lenders for the lender's failure to comply with Ability-to-Repay Rule.

   i. Consumer has 3 years from closing to file suit for lender's failure to comply with Ability-to-Repay rule.

   ii. Potential recovery for the consumer: actual damages, statutory damages of all points, fees and finance charges paid by the borrower, a $4000 penalty, attorney's fees and court costs.

   iii. After the three year Statute of Limitations has passed, the borrower may still assert the lender's violation of the Ability-to-Repay Rule as an offset or recoupment in a foreclosure or other collection action by the lender.

9) Qualified Mortgage ("QM") – creates a Safe Harbor/Rebuttable Presumption against a consumer's lawsuit, depending on whether the loan is a higher-priced Qualified Mortgage. If the QM loan is not higher-priced, than a court would conclusively presume that the lender complied with the ATR Rule.

10) A loan is "higher priced" if the APR exceeds the APOR by 1.5% for first-liens and 3.5% for subordinate liens. See www.ffiec.gov/ratespread

11) The QM Rule prohibits certain risky loan features and practices, such as negative amortization, interest only and loan terms longer than 30 years.

12) Fannie Mae and Freddie Mac have announced that they will only purchase QMs.

13) Elements of a QM - in addition to the prohibition of risky loan features and practices (no negative amortization, no interest only, no term longer than 30 years),

i. Points and fees paid by consumer cannot exceed:

- 3% of the total loan amount for loans over $100,000.
- $3,000.00 for loans from $60,000-$100.000
- 5% for loans of $20,000-$60,000
- $1000.00 for loans of $12,500.00-$20,000.00
- 8% for loans less than $12,500.00

ii. The Debt-to-Income Ratio may not exceed 43%. This ratio may be exceeded if the loan is eligible for purchase by Fannie Mae/Freddie Mac or is eligible for programs of HUD, the VA, the USDA or the Rural Housing Service

14) Small Creditor Qualified Mortgage

i. A "Small Creditor" is a lender with assets less than $2 billion at the end of the last calendar year and who originated no more than 500 first-lien closed-end residential mortgages in the preceding calendar year.

ii. A Small Creditor must underwrite the loan based on a fully-amortizing payment schedule using maximum rate for first 5 years.

iii. The Small Creditor must verify consumer's income or assets, debts, alimony and child support.

iv. Although the Small Creditor should consider the consumer's debt-to-income ratio, they are not limited by the 43% Debt-to-Income ratio.

v. The loan may not be subject to a forward commitment to sell the loan after closing.

vi. The Small Creditor must keep the QM loan in its portfolio for at least 3 years (or sell it to a Small Creditor)

vii. Small Creditor Balloon-Payment Qualified Mortgage- 2 year transition period (until January 10, 2016) Small Creditors may make Balloon-Payment QMs at least until 1/10/16

15) Record Keeping- lenders must keep `evidence that they complied with the ATR/QM Rule for <u>three years</u> after closing.

16) Fair Lending Concerns if Lenders chose to make only Qualified Mortgages - "Disparate Impact"

Interagency Statement on Fair Lending Compliance and the Ability-to-Repay and Qualified Mortgage Standards Rule

> *"In the Agencies' view, the requirements of the Ability-to-Repay Rule and ECOA are compatible…ECOA and Regulation B promote creditors acting on the basis of their legitimate business needs. Viewed in this context…the Agencies do not anticipate that a creditor's decision to offer only Qualified Mortgages would, absent other factors, elevate a supervised institution fair lending risk."*