

CFPB Eases the Requirements for Lenders to Make Qualified Mortgages Under the Ability-to-Repay Rule

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Financial institutions have been provided significant relief in complying with one of the key regulatory provisions adopted as a result of the 2008 financial crisis: the prohibition on making a residential mortgage loan unless the lender has a reasonable basis to believe the borrower can repay the loan. The relief is in the form of broader categories of qualified mortgages (“QMs”), which are loans that meet certain criteria and are deemed to meet the ability-to-repay requirements.

The Consumer Financial Protection Bureau (the “CFPB”) has issued two final rules amending the Ability-to-Repay/Qualified Mortgage Rule (“ATR/QM Rule”):

- General QM Final Rule. Among other things, the General QM Final Rule adopts price-based thresholds, replacing the existing 43 percent debt-to-income (“DTI”) ratio limit for the purpose of determining whether a loan meets the QM standards and can obtain protection from liability under the ability-to-repay requirements.
- Seasoned QM Final Rule. The Seasoned QM Final Rule creates a new QM category called the Seasoned QM for first-lien, fixed-rate covered loans that have been held in portfolio by a lender for at least three years and meet certain requirements.

Both final rules take effect on March 1, 2021, although the General QM Final Rule’s mandatory compliance date is July 1, 2021.

Background

Financial institutions are generally required to make a reasonable, good faith determination of a consumer’s ability to repay a residential mortgage loan (“Covered Transaction”).^[1] Lenders originating non-higher-priced QMs fall under the safe harbor, and are deemed to comply with the ability-to-repay requirements. QMs that are higher-priced have a rebuttable presumption of compliance with the ability-to-repay requirements, but consumers can rebut that presumption.^[2]

General QMs

There are several QM categories. One such category is the General QM. Pursuant to the 2013 final rule amending the CFPB's Regulation Z, a loan is a General QM if it meets all of the following requirements:

- The loan does not have negative-amortization, interest-only, or balloon-payment features;
- The loan term does not exceed 30 years;
- The points and fees do not exceed specified limits;
- The lender underwrites the loan based on a fully amortizing schedule using the maximum rate permitted during the first five years;
- The lender considers and verifies the consumer's income and debt obligations in accordance with Regulation Z's Appendix Q^[3]; and
- The consumer's DTI ratio is no more than 43 percent, determined in accordance with Appendix Q.

GSE QMs

Another category of QMs consists of loans that are eligible for purchase or guarantee by either the Federal National Mortgage Association ("Fannie Mae") or the Federal Home Loan Mortgage Corporation ("Freddie Mac") (collectively, "government-sponsored enterprises" or "GSEs"), while operating under the conservatorship or receivership of the Federal Housing Finance Agency ("FHFA"). The sunset date for temporary GSE QMs was set for January 10, 2021 (or when the GSEs cease to operate under conservatorship). In a final rule released on October 20, 2020, the CFPB extended the temporary GSE QMs to expire on the earlier of July 1, 2021 or when the GSEs cease to operate under the conservatorship of the FHFA.

EGRRCPA QMs

The Economic Growth, Regulatory Relief, and Consumer Protection Act ("EGRRCPA") was signed into law on May 24, 2018. Section 101 of the EGRRCPA amended the Truth in Lending Act ("TILA") to provide protection from liability for insured depository institutions with assets below \$10 billion with respect to certain ability-to-repay requirements ("EGRRCPA QMs").^[4] Such portfolio lenders can issue an EGRRCPA QM (which does not have a 43 percent DTI limit) provided that all of the following requirements are met:

1. The residential mortgage loan is originated and retained in portfolio by a covered institution (insured depository institutions or insured credit unions with less than \$10 billion in total consolidated assets, together with their affiliates);
2. The transaction is in compliance with the limitations with respect to prepayment penalties applicable to other qualified mortgages;
3. The total points and fees do not exceed three percent of the total loan amount;
4. The transaction does not have negative amortization or interest-only features; and
5. For the protection from liability to apply, the lender must consider and document the debt, income, and financial resources of the consumer.

General QM Final Rule

Among other things, the General QM Final Rule removes the 43 percent DTI limit and replaces it with price-based thresholds, removes Appendix Q, and maintains the "consider and verify" requirements (as discussed in further

detail below).

Price-Based Thresholds

Under the General QM Final Rule, one of the qualification standards for a General QM is that the annual percentage rate (“APR”) must not exceed the average prime offer rate (“APOR”) for a comparable transaction by more than the applicable threshold as of the date the interest rate is set. These applicable thresholds are set forth below:

- For a first-lien Covered Transaction with a loan amount greater than or equal to \$110,260: 2.25 percentage points;
- For a first-lien Covered Transaction with a loan amount greater than or equal to \$66,156 but less than \$110,260: 3.50 percentage points;
- For a first-lien Covered Transaction with a loan amount less than \$66,156: 50 percentage points;
- For a Covered Transaction secured by a manufactured home with a loan amount less than \$110,260: 6.50 percentage points;
- For a Covered Transaction secured by a manufactured home with a loan amount equal to or greater than \$110,260: 2.25 percentage points;
- For a subordinate-lien Covered Transaction with a loan amount greater than or equal to \$66,156: 3.50 percentage points; and
- For a subordinate-lien Covered Transaction with a loan amount less than \$66,156: 6.50 percentage points.^[5]

This price-based test provides higher thresholds for loans with smaller loan amounts and for subordinate-lien transactions. For example, under the new rule, the General QM protection could extend to a first lien or subordinate-lien loan with a loan amount of \$66,156 or less, and an APR of 6.50 or more percentage points above the APOR.

On the other hand, the new price-based test could limit the APR threshold for the rebuttable presumption of compliance with the ability-to-repay requirements. For example, assuming that other conditions are met, a higher priced, first-lien loan in the amount of \$110,260 or more and with an APR of 2.50 percentage points or more above the APOR could still be considered a QM and qualify for the rebuttable presumption under current rules. However, such loan would not meet the QM definition and would not qualify for the rebuttable presumption under the new General QM Final Rule.

Please note that for General QM loans for which the interest rate may or will change within the first five years after the date on which the first regular periodic payment will be due, lenders must treat the maximum interest rate that may apply during that five-year period as the interest rate for the full term of the loan when determining the APR for purposes of these thresholds.

Consider and Verify Requirements

The General QM Final Rule maintains the requirement for lenders to meet the “consider and verify” requirements at or before a loan’s consummation. Specifically, lenders must consider and verify the consumer’s current or reasonably expected income or assets (other than the value of the dwelling that secures the loan and any real

property attached to that dwelling), debt obligations, alimony, and child support. Additionally, lenders must consider the DTI ratio or residual income in accordance with the ability-to-repay requirements under Regulation Z in this regard. Lenders will no longer be required to comply with Appendix Q in determining monthly debt and income under the new rule. The General QM Final Rule does not prescribe a particular threshold or method of underwriting.

- To meet the requirement to consider current or reasonably expected income or assets, a lender must also maintain written policies and procedures and retain related records. Related documents may include an underwriter worksheet or a final automated underwriting system certification, in combination with applicable underwriting standards and any applicable exceptions, that shows how these required factors were taken into account in the ability-to-repay determination.
- To meet the “verify” requirement, lenders must use reasonably reliable third-party records. There is a safe harbor for compliance upon satisfaction of the verification standards in one or more specified manuals.[\[6\]](#)

Seasoned QM Final Rule

The Seasoned QM Final Rule creates a new category of QM.

Qualification Standards

A first-lien, fixed-rate Covered Transaction can earn “seasoned” QM status if all of the following requirements are met:

1. There are certain requirements on product features: (1) the periodic payments must be regular, substantially equal and fully amortizing; (2) no negative-amortization, interest-only, or balloon-payment features; and (3) the loan term may not exceed 30 years.
 - The Seasoned QM Final Rule does not prohibit a qualifying change that is entered into during or after a temporary payment accommodation in connection with a disaster or pandemic-related national emergency, even if such a qualifying change involves a balloon payment or lengthened loan term.
2. Points and fees do not exceed specified limits for a QM loan.[\[7\]](#)
3. The loan is not a high-cost loan under Regulation Z.[\[8\]](#)
4. The lender meets the “consider and verify” standards as required under the General QM Final Rule.
5. The loan has been held in portfolio by the originating lender or first purchaser for a 36-month period (the seasoning period).
6. At the end of the 36-month seasoning period, the loan can have no more than two 30-day delinquencies and no 60-day delinquencies.
 - Subject to certain exceptions, “seasoning period” generally means a period of 36 months beginning on the date on which the first periodic payment is due after consummation of the Covered Transaction.
 - If there is a delinquency of 30 days or more at the end of the final month of the seasoning period, the seasoning period is extended until there is no delinquency.
 - The seasoning period does not include any period during which the consumer is in a temporary payment accommodation extended in connection with a disaster or pandemic-related national

emergency, provided that there is a qualifying change. The seasoning period can only resume after the temporary payment accommodation if any delinquency is cured either pursuant to the original terms or through a qualifying change.

7. Legal title of the loan is not sold, assigned or otherwise transferred before the end of the 36-month seasoning period, except for the following exceptions:

- The transaction is required pursuant to certain supervisory sales;
- The transaction is in connection with certain mergers or acquisitions; or
- The loan may be sold, assigned, or otherwise transferred once before the end of the seasoning period, provided that the loan is not securitized as part of the sale, assignment, or transfer or at any other time before the end of the seasoning period. This means that a one-time transfer is generally permitted before the end of the seasoning period. Until the end of the seasoning period, a purchaser that acquires a loan pursuant to this exception may not subsequently transfer the loan to any other entity and maintain the loan's eligibility to become a Seasoned QM unless one of the other two exceptions applies.

8. Subject to the third exception described directly above with respect to transfer of the loan, the loan cannot at consummation be subject to a commitment to be acquired by another person.

Safe Harbor Protection

Under existing rules, in order to qualify for the QM safe harbor, a QM cannot be higher-priced; higher-priced QMs would not qualify for the QM safe harbor and can only get a rebuttable presumption of compliance with the ability-to-repay requirements.

To encourage lenders to extend credit to consumers whose loans may fall outside of the QM safe harbor at consummation, but who nonetheless have the ability to repay, the CFPB recognizes a safe harbor of compliance under the ability-to-repay requirements for Seasoned QMs, regardless of whether the loan is a higher-priced loan.

Relation to Other QMs Such as EGRRCPA QMs

The CFPB has noted in the Seasoned QM Final Rule that some transactions can fall within the scope of multiple QM categories. For instance, a loan that qualifies for a Seasoned QM status after the seasoning period might have been eligible as a QM at consummation under both the General QM and the EGRRCPA QM definitions.

Each QM category imposes different qualification standards and provides a presumption of compliance under the ability-to-repay requirements. For example, the EGRRCPA QM provides a presumption of compliance starting at consummation and is available to insured depository institutions and insured credit unions with assets below \$10 billion who hold those loans in portfolio. Both fixed and variable rate mortgages, as well as subordinate-lien loans can earn EGRRCPA QM status. Additionally, there is no post-consummation loan performance requirement. The Seasoned QM, by contrast, is not limited by lender's asset size, and is available only for fixed-rate, first-lien loans that meet a portfolio requirement, and only after a seasoning period during which the loans must meet performance requirements.

More Information

The General QM Final Rule is available [here](#). The Seasoned QM Final Rule can be found [here](#). If you have any questions regarding these final rules, please feel free to contact Joseph D. Simon at (516) 357-3710 or via email at jsimon@cullenllp.com, Kevin Patterson at (516) 296-9196 or via email at kpatterson@cullenllp.com, Elizabeth A. Murphy at (516) 296-9154, or via email at emurphy@cullenllp.com, or Mandy Xu at (516) 357-3850 or via email at mxu@cullenllp.com.

Please note that this is a general overview of the two final rules and does not constitute legal advice.

Footnotes

[1] The ATR/QM Rule applies to almost all closed-end consumer credit transactions secured by a dwelling including any real property attached to the dwelling. The ATR/QM Rule is not limited to first liens or to loans on primary residences. The ATR/QM Rule does not apply to open-end credit plans (such as home equity lines of credit); time-share plans; reverse mortgages; temporary or bridge loans with terms of 12 months or less; a construction phase of 12 months or less of a construction-to permanent loan; or consumer credit transactions secured by vacant land.

[2] Under the existing ATR/QM Rule, a higher-priced Covered Transaction generally means a Covered Transaction with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by 1.5 or more percentage points for a first-lien Covered Transaction; by 3.5 or more percentage points for a first-lien Covered Transaction that is a small creditor portfolio QM, temporary balloon-payment QM, or balloon-payment QM; or by 3.5 or more percentage points for a subordinate-lien Covered Transaction.

[3] Regulation Z Appendix Q sets forth specific standards for determining monthly debt and income.

[4] Transfer of the loans is permitted in certain limited circumstances.

[5] All of the dollar amounts are indexed for inflation.

[6] These standards include relevant provisions in specified versions of the Fannie Mae Single Family Selling Guide, the Freddie Mac Single-Family Seller/Servicer Guide, the FHA's Single Family Housing Policy Handbook, the VA's Lenders Handbook, and the USDA's Field Office Handbook for the Direct Single Family Housing Program and Handbook for the Single Family Guaranteed Loan Program.

[7] Generally, the total points and fees cannot exceed 3 percent of the total loan amount for a loan amount greater than or equal to \$110,260. (All figures reflect 2021 adjustment).

[8] Subject to certain exceptions, a high-cost mortgage is any consumer credit transaction that is secured by the consumer's principal dwelling, and in which:

- The APR applicable to the transaction will exceed the APOR for a comparable transaction by more than: 6.5 percentage points for a first-lien transaction; 8.5 percentage points for a first-lien transaction if the

dwelling is personal property and the loan amount is less than \$50,000; or 8.5 percentage points for a subordinate-lien transaction; or

- The transaction's total points and fees will exceed: 5 percent of the total loan amount for a transaction with a loan amount of \$22,052 or more; or the lesser of 8 percent of the total loan amount or \$1,103 for a transaction with a loan amount of less than \$22,052; or
- Under the terms of the loan contract or open-end credit agreement, the creditor can charge a prepayment penalty more than 36 months after consummation or account opening, or prepayment penalties that can exceed, in total, more than 2 percent of the amount prepaid. (All figures reflect 2021 adjustment).

Practices

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