

MEMORANDUM

To: Members of the Committee on Financial Services
From: Financial Services Committee Majority Staff
Date: June 13, 2013
Subject: June 18, 2013 Subcommittee on Financial Institutions and Consumer Credit Hearing on “Examining How the Dodd-Frank Act Hampers Home Ownership”

The Subcommittee on Financial Institutions and Consumer Credit will hold a hearing on “Examining How the Dodd-Frank Act Hampers Home Ownership,” at 10:00 a.m. on Tuesday, June 18, 2013, in Room 2128 of the Rayburn House Office Building. This will be a one-panel hearing with the following witnesses:

- Mr. Charles A. Vice, Commissioner, Kentucky Department of Financial Institutions, on behalf of the Conference of State Bank Supervisors
- Mr. James C. Gardill, Chairman of the Board, WesBanco, Inc., on behalf of the American Bankers Association
- Mr. Jerry Reed, Chief Lending Officer, Alaska USA Federal Credit Union, of behalf of the Credit Union National Association
- Ms. Debra W. Still, CMB, Chairman, Mortgage Bankers Association
- Mr. Gary Thomas, President, National Association of Realtors
- Democratic Witness TBD

This hearing continues the Subcommittee’s study of the impact of the Qualified Mortgage (“QM”) rule recently issued by the Bureau of Consumer Financial Protection (CFPB). The Subcommittee held its first hearing on this subject on May 21.

The Dodd-Frank Act and Residential Mortgages

Title XIV of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P. L. 111-203) made substantial changes to the mortgage lending marketplace. Section 1411 of the Act requires mortgage lenders to determine at the time a loan is made that the borrower has a reasonable ability to repay it. Section 1411 specifies that in determining whether the borrower has the ability to repay the loan, lenders

must consider “the consumer’s credit history, current income, expected income the consumer is reasonably assured or receiving, current obligations, debt-to-income ratio or the residual income the consumer will have after paying non-mortgage debt and mortgage-related obligations, employment status, and other financial resources.” If a lender fails to determine that the borrower has the ability to repay the loan, the lender is subject to statutory damages and potential class action liability. In addition, the Dodd-Frank Act permits borrowers to raise the lender’s failure to satisfy the ability to repay requirement as a defense in foreclosure proceedings.

To mitigate the potential liability lenders face, section 1412 creates a regime under which lenders may presume that a mortgage meets the ability to repay requirement if it is a “qualified mortgage.” The Dodd-Frank Act lists illustrative criteria for mortgages to be considered QMs, but delegates to the Federal Reserve Board the authority to issue regulations that specifically define a qualified mortgage.¹ The Federal Reserve Board is permitted to prescribe regulations that revise, add to, or subtract from the criteria that define a QM if necessary to ensure that responsible, affordable mortgage credit remains available to consumers. The responsibility for finalizing the QM rule transferred from the Federal Reserve Board to the Consumer Financial Protection Bureau (CFPB) on July 21, 2011.

The Rulemaking Process

On April 19, 2011, the Federal Reserve Board proposed a rule to implement Dodd-Frank’s ability to repay requirements.² The Federal Reserve’s proposal would have required creditors to determine a consumer’s ability to repay a mortgage before making the loan and would have established minimum mortgage underwriting standards. The proposal applied to all consumer mortgages and provided creditors with four options for complying with the ability to repay requirement: (1) by considering and verifying specified underwriting factors, such as the consumer’s income or assets; (2) by making a “qualified mortgage,” which provides the creditor with special protection from liability, if the loan does not have certain features; (3) for creditors operating predominantly in rural or underserved areas, by making a balloon-payment qualified mortgage; and (4) by refinancing a

¹ Section 1412 lists the following as possible features of Qualified Mortgages: (1) no negative amortization; (2) no balloon payments (except in rural or underserved areas); (3) no “interest only” payments; (4) income and financial resources of the borrower are verified and documented; (5) the loan is underwritten based on payments reflecting full amortization and takes into consideration all mortgage-related obligations, such as taxes, property insurance, and assessments; (6) variable rate loans are underwritten based on the maximum rate permitted in the first five years and a payment schedule that reflects full amortization; (7) the loan complies with any regulatory guidelines on debt-to-income ratios; (8) total points and fees generally do not exceed 3 percent of total loan amount; and (9) the term does not exceed 30 years, unless this limit is extended by regulations.

² Board of Governors of the Federal Reserve System, Press Release, April 19, 2011, available at <http://www.federalreserve.gov/newsevents/press/bcreg/20110419a.htm>.

“non-standard mortgage” with risky features into a more stable “standard mortgage” with a lower monthly payment.

On May 31, 2012, the CFPB announced it was re-opening the public comment period to seek additional input on a number of topics, most notably the litigation risks that could potentially arise from the new requirements.³

On January 10, 2013, the CFPB issued a final rule implementing the provisions of sections 1411 and 1412, in addition to section 1414, which limits prepayment penalties.⁴ The final rule details eight minimum underwriting factors for creditors making ability to repay determinations: (1) current or reasonably expected income or assets; (2) current employment status; (3) the monthly payment of the mortgage; (4) the monthly payment on any simultaneous loan; (5) the monthly payment for mortgage-related obligations; (6) current debt obligations, alimony, and child support; (7) the monthly debt-to-income ratio or residual income; and (8) credit history.

According to the CFPB, the final rule provides a safe harbor for loans that satisfy the definition of a qualified mortgage and are not “higher-priced,” and it provides a rebuttable presumption for higher-priced mortgage loans. The rule generally excludes from the definition of qualified mortgages those loans with negative amortization, interest-only payments, balloon payments, or terms exceeding 30 years. Also generally excluded from the definition are loans on which the points and fees paid by the consumer at closing exceed three percent of the total loan amount. The rule establishes general underwriting criteria for qualified mortgages, including a requirement that the consumer have a total debt-to-income ratio that is less than or equal to 43 percent. Finally, the rule permits certain balloon-payment loans to be treated as qualified mortgages if they are originated and held in portfolio by small creditors operating predominantly in rural or underserved areas.

On May 2, 2013, the CFPB published a proposal to amend the final ability to repay rule.⁵ The proposal would (1) amend Appendix Q to clarify its application and

³ “Consumer Financial Protection Bureau seeks further comment on Ability-to-Repay mortgage rule,” Consumer Financial Protection Bureau, May 31, 2012, available at <http://www.consumerfinance.gov/pressreleases/consumer-financial-protection-bureau-seeks-further-comment-on-ability-to-repay-mortgage-rule/>.

⁴ Ability to Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), Consumer Financial Protection Bureau, January 10, 2013, available at <http://www.consumerfinance.gov/regulations/ability-to-repay-and-qualified-mortgage-standards-under-the-truth-in-lending-act-regulation-z/>.

⁵ Consumer Financial Protection Bureau, “Amendments to the 2013 Mortgage Rules under the Real Estate Settlement Procedure Act (Regulation X) and the Truth in Lending Act (Regulation Z),” available at: http://files.consumerfinance.gov/f/201304_cfpb_proposed-rule_amending-atr-qm-and-servicing-mortgage-rules.pdf.

to make it easier for lenders to comply with the rule's requirements when determining the debt-to-income ratio, and (2) clarify the extent to which a creditor may make a qualified mortgage determination based on whether a loan was purchased, guaranteed, or eligible for insurance by a government-sponsored enterprise or federal agency. The comment period for the proposed amendments closed on June 3, 2013.

On May 29, 2013, the CFPB adopted a number of amendments to the QM rule that were proposed concurrently with the final rule in January.⁶ The amendments would (1) exempt from the final rule certain nonprofit and community-based lenders that work to help low- and moderate-income consumers obtain affordable housing; (2) extend qualified mortgage status to loans made by certain small creditors who hold these loans in portfolio, provide a two-year transition period during which certain small creditors may issue balloon loans, and allow them to charge a higher annual percentage rate for first-lien loans while maintaining a safe harbor; and (3) exclude from the 3 percent points and fees cap compensation paid by a mortgage broker to a loan originator employee. These amendments will take effect with the ability to repay rule on January 10, 2014.

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⁶ Consumer Financial Protection Bureau, "CFPB Finalizes Amendments to Ability-to-Repay Rule," May 29, 2013, available at: <http://www.consumerfinance.gov/pressreleases/cfpb-finalizes-amendments-to-ability-to-repay-rule/>.