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COMING IN 2021: CFPB FINALIZES CHANGES TO "QUALIFIED MORTGAGE" DEFINITION AND CREATES A NEW "SEASONED QM" LOAN CATEGORY

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Summary

- 12/10/2020 - The CFPB issued final rules amending the General Qualified Mortgage loan definition in Regulation Z and, by separate rule, creating a new “Seasoned QM” loan category in Regulation Z.

- Both rules take effect sixty days from the date they are published in the Federal Register and have a mandatory compliance date of July 1, 2021.

- The CFPB is applying the mandatory compliance date to the date on which a creditor receives a consumer’s QM loan application.

- Starting on the effective date and until July 1, 2021, compliance with the General QM Final Rule is optional.

New Eligibility Requirements for General QM Loan Category

- The loan must be **fixed rate, fully amortizing** and provides for regular periodic and substantially equal monthly payments **or, in the case of adjustable-rate or step-rate mortgages:**

  (i) the loan is fully amortized,

  (ii) the loan does not allow for deferment of principal loan amount repayment (with limited exception for temporary payment accommodation in connection with a disaster or pandemic-related national emergency), and

  (iii) the loan does not have a balloon payment unless it meets the balloon payment QM requirements of 12 CFR 1026.43(f).

- The **maximum loan term** is 30 years.

- **"Total Points and Fees"** do not exceed the QM limits set forth in 12 CFR 1026.43(3)(i) (for loans over $100,000 adjusted for inflation, the limit is 3 percent of total loan amount).

New Eligibility Requirements for General QM Loan

Replacing the former 43% DTI cap, the eligible loan must now adhere to a new **Price-Based Limit** whereby the Annual Percentage Rate (APR) does not exceed the Average Prime Offer Rate (APOR) for a comparable transaction by a certain percentage points threshold. That threshold is **2.25 percentage points** for loan amounts >= $110,260 (adjusted annually for inflation). For lower loan amounts, the threshold percentage increases incrementally up to 6.5 percentage points.

(i) The threshold for **subordinate-lien covered loans is 3.5 percentage points** if the loan amount is >= **$66,156**, and increases to 6.5 percentage points if the loan amount < $66,156.

(ii) If the loan is secured by **manufactured housing that meets HUD code standards** and the loan amount is >= **$110,260**, the threshold is **2.25 percentage points**. That threshold increases to 6.5 percentage points if the loan amount < $110,260. If the manufactured housing does not meet HUD code standards, the loan is not eligible for QM treatment.

- If the loan's interest rate may or will change in the first 5 years, creditors are instructed to calculate APR for purposes of measuring this threshold by applying the highest potential or scheduled interest rate during the initial 5 years and assume that rate will apply for the full loan term.

New Eligibility Requirements for General QM Loan

(iii) If the loan's interest rate may or **will change in the first 5 years**, creditors must calculate APR for purposes of measuring this threshold by applying the highest potential or scheduled interest rate during the initial 5 years and assume that rate will apply for the full loan term.

- **Replacing the former Appendix Q underwriting standards**, the creditor must instead meet **Regulation Z "consider and verify" loan underwriting requirements**. This means the creditor must consider the consumer's current or reasonably expected income or assets other than the value of the subject dwelling, debt obligations, alimony, child support, and monthly debt-to-income ratio or residual income in order to assess the consumer's ability to repay the mortgage loan, and verify this information using third-party records that provide reasonably reliable evidence to support accuracy.

New Eligibility Requirements for General QM Loan

- The **underwriting takes into account** the monthly payment for mortgage-related obligations, using both the maximum interest rate that may apply during the first five years, and the periodic loan payments of principal and interest that will repay the loan amount over the scheduled loan term **or, for adjustable rate loans**, the outstanding principal balance over the remaining term of the loan as of the date the interest rate adjusts to the maximum interest rate, assuming the consumer will have made all required payments as due prior to that date.

Agency Loans Remain As Covered Transactions

- Loans that qualify for federally insured or guaranteed FHA, VA and USDA/RHS mortgage loan programs will remain as covered transactions under the General QM Final Rule.

Sunsetting of the Temporary QM Patch

- In 2013, the CFPB created a temporary Qualified Mortgage category for residential mortgage loans eligible for purchase by Fannie Mae or Freddie Mac while they operate under conservatorship or receivership of the Federal Housing Finance Agency (FHFA). This temporary QM category was scheduled to expire no later than January 10, 2021.

- On October 20, 2020, the CFPB extended this expiration date to align with whatever mandatory compliance date would be established in the impending Final General QM Rule.

- The December 2020 Final General QM Rule officially sunsets the Temporary QM Patch on July 1, 2021. The Temporary QM Patch category will be available only for covered transactions for which the creditor receives the consumer's application for a Fannie Mae or Freddie Mac eligible mortgage loan prior to July 1, 2021, or sooner if the GSEs exit conservatorship of FHFA at an earlier date.

QM Safe Harbor and Rebuttable Presumption Thresholds Remain

- The Final General QM Rule does not change the percentage thresholds for "Safe Harbor" vs "Rebuttable Presumption" treatment.

- **To be eligible for "Safe Harbor" liability protection** (a conclusive presumption of meeting Regulation Z's Ability To Repay loan underwriting standard), the APR on a first lien QM loan cannot exceed the APOR for a comparable transaction by more than **1.5 percentage points**. For subordinate lien QM loans, the APR cannot exceed the APOR by more than **3.5 percentage points**.

The New "Seasoned QM" Loan Category Requirements

To qualify as a **Seasoned QM**, a mortgage loan must meet **loan eligibility requirements** that are similar to General QM with slight variation <u>plus</u> the loan must be held in the lender's portfolio for three years (a **36-month seasoning period**), and meet certain **performance requirements and portfolio requirements**.

- It is a first lien fixed rate loan with substantially equal periodic payments (with certain limited allowance for temporary payment accommodation in connection with a disaster or pandemic-related national emergency).
- It is fully amortizing.
- It does not have a balloon payment unless it meets the balloon payment QM requirements of 12 CFR 1026.43(f).
- The loan term does not exceed 30 years.

The New "Seasoned QM" Loan Category Requirements

- Points and fees do not exceed the QM points and limits set forth in 12 CFR 1026.43(3)(i) (for loans over $100,000 adjusted for inflation, the limit is 3 percent of total loan amount).
- It is not a high-cost loan as defined in 12 CFR 1026.32(a).
- The underwriting takes into account the monthly payment for mortgage-related obligations, using:

  (i) The maximum interest rate that may apply during the first five years;

  (ii) Periodic payments of principal and interest that will repay either:

  - The outstanding principal balance over the remaining term of the loan as of the date the interest rate adjusts to the maximum interest rate, assuming the consumer will have made all required payments as due prior to that date; or
  - The loan amount over the loan term;

The New "Seasoned QM" Loan Category Requirements

- At or before consummation, the creditor:

(i) Considers the consumer's current or reasonably expected income or assets other than the value of the dwelling that secures the loan, debt obligations, alimony, child support, and monthly debt-to-income ratio or residual income.

(ii) Uses reasonably reliable third party records to verify the consumer's:

- Current or reasonably expected income or assets other than the value of the dwelling that secures the loan using reasonably reliable evidence from third-party records; and
- Current debt obligations, alimony, and child support using reasonably reliable third-party records.

"Seasoned QM" Performance Requirements

- The loan must have no more than two 30-day delinquencies and no delinquencies of 60 or more days during the three-year seasoning period.

- There are exceptions.
  - ❑ If a loan is delinquent at the end of the seasoning period due to a disaster or pandemic-related national emergency, the loan may still be a Seasoned QM if certain conditions are met. Any temporary payment accommodation extended to a borrower will not be counted toward the seasoning period.
  - ❑ If a loan is 30 days or more delinquent at the end of the seasoning period, the seasoning period is not considered ended until the delinquency is cured.

- A creditor can generally accept deficient payments within a payment tolerance of $50 on up to three occasions during the seasoning period.

“Seasoned QM” Portfolio Requirements

- To be a Seasoned QM, the covered transaction must not be subject, at consummation, to a commitment to be acquired by another person.
- In addition, legal title to the loan cannot be transferred to another person before the end of the 3-year seasoning period.
- There are exceptions to both rules that will allow limited opportunity for loan sale, assignment or transfer prior to the end of the seasoning period:
  - — Creditor merger or acquisition.
  - — The transaction may be transferred pursuant to a capital restoration plan or other prompt corrective action under 12 U.S.C. 1831o, actions or instructions of any person acting as conservator, receiver, or bankruptcy trustee, an order of a State or Federal government agency with jurisdiction to examine the creditor pursuant to State or Federal law, or an agreement between the creditor and such an agency.
  - —The transaction may be transferred once before the end of the seasoning period, provided that the covered transaction is not securitized as part of the transfer or at any other time before the end of the seasoning period.

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Michael Flynn is a member of the Firm's Commercial Finance Practice Group and Mortgage Banking Group, and Co-Chair of Buchalter's Financial Services Regulatory Group, and its Title Insurance & Escrow Industry Group in the Los Angeles office. Mr. Flynn applies his unique background as the former Acting General Counsel of HUD, and the former General Counsel of PNC Mortgage and Flagstar Bank, to counsel clients on a variety of regulatory, mortgage, consumer financial services, FinTech and real estate matters.

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Melissa Richards, CMB is a California licensed attorney with a national practice specializing in federal and multistate compliance, licensing and enterprise risk management for the financial services industry. Her clients are engaged in residential and commercial mortgage, fintech, licensed non-depository and depository institution consumer and commercial lending, either directly or in supporting vendor roles. Ms. Richards has both outside counsel experience as well as general counsel experience. From 2012-2018, Ms. Richards served as the Chief Legal & Risk Officer of a mid-size independent mortgage company ranked as one of *Scotsman Guide's Top 15 Mortgage Lenders* in 2018-2019.

Ms. Richards has served in leadership for the California Mortgage Bankers Association, both as a three-term Director (1999-2008) and as its General Counsel (2002-2008). For the Mortgage Bankers Association, Ms. Richards received her CMB designation in 2009 and served as Co-Chair of the 2017 MBA RESBOG Task Force on CFPB Regulatory Clarity and Enforcement (CFPB 2.0). Ms. Richards is a frequent national speaker on federal and state compliance current events affecting the financial services industry, including implementation and enforcement of California's Consumer Privacy Act and implementing state AG regulations.