

MORTGAGE LENDING SUBCOMITTEE AGENDA

Jeffrey Ledbetter, Chair
Andrew Budish, Vice Chair
Larry Platt, Counsel

1. Satisfying the ATR for Non-QM Loans – Larry Platt

2. VA Inspector General Subpoena of Lenders for Underwriting of Loans – Larry Platt

3. Release of HMDA LAR Data by the CFPB– Jeff Ledbetter

<https://www.consumerfinance.gov/about-us/newsroom/hmda-modified-loan-application-registers-released/>

4. HUD FHA Action Against Facebook – Jeff Ledbetter

https://www.hud.gov/press/press_releases_media_advisories/HUD_No_18_085

5. CFPB Supervisory Highlights – Jeff Ledbetter

https://files.consumerfinance.gov/f/documents/cfpb_supervisory-highlights_issue-18_032019.pdf



Satisfying the Ability to Repay Requirements for Non-QM Residential Mortgage Loans

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MORTGAGE LENDING SUBCOMMITTEE

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Various Types of Consumer Credit Ability to Repay Requirements

Credit Cards

12 CFR 1026.51(a)(i) Consideration of ability to pay: A card issuer must not open a credit card account for a consumer under an open-end (not home-secured) consumer credit plan, or increase any credit limit applicable to such account, unless the card issuer considers the consumer's ability to make the required minimum periodic payments under the terms of the account based on the consumer's income or assets and the consumer's current obligations.

UDAAP

CFPB Supervision and Examination Manual/Risk Assessment Template/Inherent UDAAP Risk in Nature and Structure of Products: Credit products are not underwritten based upon the likely ability of the consumer to make the required (or, in the case adjustable rate products, potentially required) payments over the term of the loans.

Various Types of Consumer Credit Ability to Repay Requirements

UDAP (Massachusetts)

940 CMR 8.06(15) (under 93A): It is an unfair or deceptive act or practice for a mortgage broker to arrange or mortgage lender to make a mortgage loan unless the mortgage broker or lender, based on information known at the time the loan is made, reasonably believes at the time the loan is expected to be made that the borrower will be able to repay the loan based upon a consideration of the borrower's income, assets, obligations, employment status, credit history, and financial resources, not limited to the borrower's equity in the dwelling which secures repayment of the loan (subject, however, to the treatment of No Income Loan Products in 940 CMR 8.06(16)).

Small Dollar Loans (Eliminated in Revised Proposal)

§ 1041.4 Identification of unfair and abusive practice.

It is an unfair and abusive practice for a lender to make covered short-term loans or covered longer-term balloon-payment loans without reasonably determining that the consumers will have the ability to repay the loans according to their terms.

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Summary of CFPB Ability to Repay Requirements for Residential Mortgage Loans

- In accordance with regulations prescribed by the Bureau, 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.
- Not willingness, but ability, to repay. (LTV not relevant)
- Exception for QM

Footer

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Loans Subject to Ability to Repay Rule

- ATR applies to consumer-purpose, closed-end loans secured by a dwelling
 - First and junior lien, home-purchase, refinance and home equity loans

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Requirements to Satisfy ATR

- Creditor must verify consumers' ATR using reasonably reliable third-party records
- Bureau does not dictate a particular underwriting model
- At a minimum creditors must consider 8 underwriting factors:
 - Current or reasonably expected income or assets
 - Current employment status
 - Monthly payment on covered transaction
 - Monthly payment on simultaneous loan
 - Monthly payment for mortgage-related obligations
 - Current debt obligations, alimony, child support
 - Monthly debt-to-income ratio or residual income
 - Credit history

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Violation of Ability to Repay Rule

Liability / Penalties

- CFPB - Authority to issue cease and desist orders and impose civil monetary penalties
- Federal Private Right of Action – Affirmative action against creditor (not assignees) for:
 - actual damages
 - statutory damages (individual and class actions)
 - special damages equal to all finance charges and fees (unless failure not material)
 - costs and attorney fees

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Violation of Ability to Repay Rule

Liability / Penalties

- Affirmative claims - Three year statute of limitations
- Defensive claims in foreclosure - by recoupment or set off
 - No 3-year statute of limitations
 - TILA damages, but special statutory damages limited to no more than 3 years of finance charges and fees
 - Applies to assignees

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Exemption from Ability to Repay Rule

Legal Consequences of "Exemption" for Qualified Mortgages

- Safe Harbor – QMs that are not higher priced are conclusively deemed to comply with the ability-to-repay requirements
- Rebuttable Presumption – QMs that are higher priced are presumed to comply with ability-to-repay requirements
 - First Liens: APR 1.5 over APOR
 - Second Liens: APR 3.5 over APOR
 - To rebut presumption: Borrower must prove that creditor did not make reasonable, good faith determination of repayment ability, because consumer's income, debt, alimony, child support, and monthly payments would leave consumer with insufficient residual income or assets to meet living expenses of which the creditor was aware
- Risk Remains – Borrower can still challenge whether a loan is a QM loan (e.g., 3 points, 43% D-T-I)

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Ability to Repay Rule

"Exemption" for Qualified Mortgages

- A covered transaction with following characteristics:
 - Regular periodic payments (i.e., substantially equal – no neg am, deferral of principal repayments, or balloons, with limited exceptions)
 - Loan term not over 30 years
 - Total points and fees do not exceed 3% (different thresholds for loans under \$100,000)
 - Must consider monthly payments for property taxes; premiums for insurance required by the creditor; fees and special assessments
 - Must consider maximum rate during the first 5 years after the first regular periodic payment will be due
 - Must consider periodic payments of principal and interest that will repay the loan amount over the loan term (or the outstanding principal balance over the remaining term once the rate adjusts to its maximum)

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Ability to Repay Rule

"Exemption" for Qualified Mortgages

- Must consider and verify, in accordance with Appendix Q:
 - Current or reasonably expected income or assets
 - Current debt obligations, alimony, child support
 - Verification = reasonably reliable third-party records (rule provides examples)
- Monthly DTI at consummation does not exceed 43% (using App. Q)
 - Must include monthly mortgage-related obligations and simultaneous loans about which creditor knows/has reason to know

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Ability to Repay Rule

"Exemption" for Qualified Mortgages

- Total Points and Fees – 3% (different for loans with UPB under \$60,000)

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Ability to Repay Rule

Alternative/Temporary Qualified Mortgage

- Fannie Mae or Freddie Mac: Loans eligible to be purchased or guaranteed by GSEs while under conservatorship or receivership (or limited life successor entity)
 - Desktop Underwriter “Approve/Eligible”
 - Loan Prospector “Accept and Eligible to Purchase”
 - Conformity with Single-Family Selling Guides
- FHA, VA, USDA, RHS: Special rules for government insured or guaranteed loans.

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Grappling with ATR Underwriting Requirements for Self-Employed Borrowers in the Non-QM Space

- The crux of the issue is how to derive personal income for ATR purposes from information about the self-employed borrower’s business and how it is verified/documented. More specifically, how to determine:
 - Revenues and expenses of the business or profit generated by the business
 - Profits from the business translates into personal income for the self-employed borrower
 - Sustainability

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Grappling with ATR Underwriting Requirements for Self-Employed Borrowers in the Non-QM Space

- Compare this with Fannie Mae’s relatively detailed requirements at Fannie Mae Selling Guide B3-3.2-01: Underwriting Factors and Documentation for a Self-Employed Borrower
 - “When determining the appropriate qualifying income for a self-employed borrower, it is important to note that business income (specifically from a partnership or S corporation) reported on an individual IRS Form 1040 may not necessarily represent income that has actually been distributed to the borrower. The fundamental exercise, when conducting a self-employment income cash flow analysis, is to determine the amount of income that can be relied on by the borrower in qualifying for their personal mortgage obligation. When underwriting these borrowers, it is important to review business income distributions that have been made or could be made to these borrowers while maintaining the viability of the underlying business. This analysis includes assessing the stability of business income and the ability of the business to continue to generate sufficient income to enable these borrowers to meet their financial obligations.”

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Grappling with ATR Underwriting Requirements for Self-Employed Borrowers in the Non-QM Space

- Or Compare with Appendix Q
 - App Q does not mention bank statements at all, including for S/E borrowers.
 - It requires signed, dated, individual tax returns with all applicable schedules for two years; signed copies of business tax returns with all schedules for two years; YTD P&L statement; and balance sheet.

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Grappling with ATR Underwriting Requirements for Self-Employed Borrowers in the Non-QM Space

- On the non-QM side, companies are competing for business based on **not** requiring individual or business tax returns and have varying reliance on business bank statements. We see a wide swath of approaches with materially different degrees of riskiness.
- While the law puts the onus on the lender to figure out what is reasonable, the law doesn't compel the conclusion. Where ambiguity is inherent in the law, businesses compete on filling in the details, but many are sitting on the sidelines by virtue of the lack of clarity and the perceived risk.

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Grappling with ATR Underwriting Requirements for Self-Employed Borrowers in the Non-QM Space

- With that backdrop, there are "reasonableness" examples in the marketplace, of varying (1) underwriting/income determinations, and/or (2) third party verification and documentation.
 - Borrower prepared P&L with evidence of underlying deposits into business bank accounts through 12 months of business bank statements, but no evidence of actual expenses, but rather fixed expense ratios (i.e., no underwriting of outflows; only reconciliation of deposits to revenue). One then infers business profit translates into personal income.
 - Sole proprietors providing personal bank statements and CPA prepared P&L (alternatively, sole props where borrower owns more than 50% of company, providing just business bank statements, rather than personal bank statements)
 - Fannie Mae VOE program without 4506T requirement even though w-2 employee
 - CPA letter based on 12 months of P&L plus 1 month of business bank statements
 - Borrower prepared P&L for 12 month period plus 1 month of business bank statements

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Grappling with ATR Underwriting Requirements for Self-Employed Borrowers in the Non-QM Space

- Open questions: (i) may personal income be derived from business profitability; and (ii) is the lender required to find evidence of a nexus between business profitability and personal income, or may it instead simply infer that profits from a business are available to pay personal expenses without having to follow the money from business account to personal account.