



COMPLIANCE CHALLENGES

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Qualified Mortgages: Present and Future

Different Rules Apply to Today's Different QMs

When explaining a lengthy and complex rulemaking process, it is tempting to look into the past and start at the beginning. However, for credit unions that simply want to understand the current boundaries of Qualified Mortgages (QMs), we should focus on the present.

In short, there are now several types of QMs from which credit unions may choose, each with its own parameters and requirements. In the future, though, all bets are off.

OLD QMs

The first QM is the one with which we are all familiar—[the 43% debt-to-income ratio (DTI) QM. While the Consumer Financial Protection Bureau (CFPB) previously considered phasing out the “old” QM, the agency’s new leadership has changed its mind.

Accordingly, a closed-end residential mortgage loan will still constitute a QM when it has:

- A DTI that does not exceed 43%.
- Underwriting in accordance with the regulation’s Appendix Q.
- Points and fees that do not exceed the threshold (generally 3%).
- No balloon payment or other non-standard payment arrangements.

If the annual percentage rate (APR) does not exceed the average prime offer rate (APOR) for a comparable transaction by 1.5 percentage points, then the QM enjoys a “safe harbor” of compliance with the federal Ability to Repay Rule. If the loan’s APR exceeds that threshold, the loan gets a rebuttable presumption of compliance with that rule.

Unless something changes, the old QM is available until October 1, 2022.

NEW QMs

A new QM category is also now available. For applications received on or after March 1, 2021, credit unions and other mortgage lenders can make QMs

without a 43% DTI cap and without following Appendix Q, so long as the APR does not exceed 2.25 percentage points over APOR (for most first-lien loans).

As above, if the APR does not exceed the APOR by 1.5 percentage points, the QM enjoys a safe harbor of compliance with the rule; otherwise, the loan gets a rebuttable presumption of compliance.

Under this new QM, the loan still must meet the “old” QM restrictions against non-standard payment features and limits on points and fees. The lender must still consider DTI (or residual income), but the regulations do not impose a cap. The lender also must still consider the consumer’s current or reasonably expected income or assets, debt obligations, alimony and child support.

While that “consider” requirement sounds familiar, the regulations specify that for new QMs, a lender must develop underwriting standards and maintain written policies and procedures for how it considers the required factors.

The lender also must, for each loan, retain documentation, like a worksheet

or automated underwriting system certification, showing how the lender considered the factors and applied its policies and procedures. The lender's policies and procedures must describe any available exceptions to the underwriting standards, and the lender must keep loan-level documentation of any exceptions on which it relies.

The lender also must verify those amounts using reasonably reliable third-party documentation. The lender is no longer stuck with the documentation requirements in Appendix Q, and instead may use any reasonable verification methods and criteria. While some lenders may welcome that flexibility, lenders also may rely on specified verification standards of Fannie Mae, Freddie Mac, the Federal Housing Administration (FHA), Department of Veterans Affairs (VA) or U.S. Department of Agriculture.

Accordingly, so long as loans stay under the 2.25 APR threshold, the new QM offers significant flexibility for credit unions to provide mortgage loans to their members. However, some work is required up front to ensure that product parameters, compensating factors and allowable exceptions are in writing, and loan-level documentation processes are in place.

AGENCY QMs

Credit unions also may still make agency QMs. The regulations continue to allow the FHA,

VA and USDA to establish their own rules for what constitutes a QM under their respective programs, and those agencies' requirements for this purpose have not changed.

However, Fannie Mae and Freddie Mac (the GSEs) have changed their requirements. The GSEs (under their regulator's orders) announced that as of July 1, 2021, they will purchase non-



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exempt mortgage loans only if they meet the new APR-based QM requirements.

In the past, particularly for certain loans with a DTI over 43%, many lenders gained QM status by relying on GSE eligibility. Going forward, the GSEs will purchase those loans only if they also meet the 2.25 APR threshold and other new QM requirements. (The GSEs also may purchase loans that meet the Small Creditor Portfolio QM criteria, described below.)

SMALL CREDITOR PORTFOLIO QMs

A "small creditor" may continue to make QMs without regard to certain old or new QM requirements, so long as the creditor retains the loans in its portfolio.

A "small creditor" is, in somewhat simplified terms, a creditor that, along with its affiliates, extended no more than 2,000 first-lien, closed-end residential mortgage loans during the preceding calendar year that were sold, assigned or otherwise transferred to, or committed to be acquired by, another person. In addition, the creditor and any lending affiliates must have total assets below a certain threshold. (For calendar year 2021, the asset threshold is \$2.23 billion.)

Although small portfolio creditors must continue to consider a consumer's current or reasonably expected income or assets, current debt obligations, alimony, child support and DTI or residual income, the creditors are not required to observe the 43% DTI cap or Appendix Q. Similarly, since March 1, 2021, they may make QMs without observing the 2.25 percentage point APR cap.

However, if the creditor sells, assigns

or otherwise transfers the loan within three years, the loan generally will lose its QM status.

In addition, those small portfolio creditors that lend in a rural or underserved area may continue to make balloon payment QMs under special regulatory provisions, without complying with the old DTI or new APR caps.

QMs IN THE FUTURE

While the CFPB (under previous leadership) wanted to eliminate the old QM (43% DTI/Appendix Q) by July 2021, the agency now believes doing so could exacerbate the economic effects of the Covid-19 pandemic. By making the old QM available until October 2022, along with the new QM, the CFPB hopes lenders will

have more tools to provide responsible, affordable mortgage credit while the economy recovers.

Of course, those additional 15 months also provide the CFPB's new leadership time to reconsider all the QM options described above. The agency expressly stated that it may revisit the old and new QM definitions, as well as the ability of certain loans to "season" into QM status after three years of timely payments.

With those potential changes looming, credit unions may want to focus on the present, and worry about the future later!



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