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EXAMINING HOW THE DODD-FRANK ACT HAMPERS HOME OWNERSHIP

HEARING

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

JUNE 18, 2013

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CONTENTS

EXAMINING HOW THE DODD-FRANK ACT HAMPERS HOME OWNERSHIP

Tuesday, June 18, 2013

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER CREDIT,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:02 a.m., in room 2128, Rayburn House Office Building, Hon. Shelley Moore Capito [chairwoman of the subcommittee] presiding.

Members present: Representatives Capito, Duffy, Miller, McHenry, Pearce, Fitzpatrick, Luetkemeyer, Pittenger, Barr, Cotton, Rothfus; Meeks, Maloney, Hinojosa, Scott, Green, Ellison, Velazquez, Lynch, Capuano, Murphy, and Heck.

Ex officio present: Representatives Hensarling and Waters.

Chairwoman CAPITO. The Subcommittee on Financial Institutions and Consumer Credit will come to order. Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

I now yield myself 2½ minutes for my opening statement.

This morning's hearing is the second installment in a series of hearings that this subcommittee is holding on the effect that the Consumer Financial Protection Bureau's (CFPB's) ability-to-repay rule will have on the availability of mortgage credit for consumers. During the last hearing, we heard from representatives from the CFPB about the status of the rule and the feedback that they were hearing. There was almost unanimous agreement from members of the subcommittee that the rule in its current form could lead to a constriction of credit when it goes into effect in January of 2014. The CFPB must give those concerns serious consideration and address them in order to avoid serious market disruption.

In the last 6 weeks, the CFPB issued amendments to the rule addressing concerns that had already been raised. Although these revisions attempt to provide clarity to lenders, the need for these changes highlights the fundamental problem with the ability-to-repay rule.

Mortgage lending can be a highly subjective business, especially in rural and underserved areas. This element of relationship-based decision-making is completely ignored by the premise of the rule. It will be nearly impossible for the CFPB to endlessly amend the rule to accommodate the ability of lenders to make these relationship-based loans. Unfortunately, the end result will be some consumers losing access to credit and the ability to own their own home.

This morning, we will hear from mortgage professionals who are best able to determine the real effects of this rule and what effects it will have on the mortgage market. We are here today to not only learn about how this rule will affect the available mortgage credit, but also to begin discussion of better ways to preserve access to mortgage credit and protect consumers.

I fear that without significant revision or repeal of this rule in its entirety, the consumers that proponents of the rule are attempting to protect will be the very consumers who are blocked out of the system. Without significant changes, consumers who live in rural areas with low property values will see a change in their availability of credit. The consequences of this rule, whether intended or unintended, will be very real to these communities. In fact, one of our witnesses today is concerned that the institution he represents may no longer be able to offer a charitable program for low-income borrowers. This program has been in existence since 1951 and has helped residents of Ohio County, West Virginia, who otherwise could not attain the goal of home ownership. This is exactly the type of case-by-case local lending that will be threatened by rigid Federal standards.

I now yield to the ranking member of the subcommittee, Mr. Meeks, for the purpose of making an opening statement.

Mr. MEEKS. Thank you, Chairwoman Capito, for holding this important hearing. Let me start by reaffirming the need and the support for the Dodd-Frank Act. No bill that I have seen in my 15 years here is perfect. But the 2008 financial crisis was a painful and regrettable demonstration of the need to reform our financial institutions, our capital markets, and our regulatory agencies, and to have laws to prevent the reoccurrence of the excessive behavior that got us here in the first place.

That is why I have remained open-minded in my search for true bipartisan solutions to address some of the shortcomings of the bill, particularly those aspects of the law that affect the most vulnerable. We need to make sure that we help our local communities and our local banks, whose activities did not blow up the global financial system, but are facing real challenges in this modest economic recovery.

I support a balanced, risk-sensitive Qualified Mortgage (QM) definition that protects consumers from predatory lending practices while also ensuring that we maintain a competitive, accessible, and liquid housing finance industry that serves all niches of the population.

This is why I cosponsored H.R. 1077 to specifically address and support home ownership and financing opportunities by first-time home buyers and low- and moderate-income families. H.R. 1077 addresses major concerns on regulatory agencies' rulemaking on Qualified Mortgages as required by Dodd-Frank and focuses on the Consumer Financial Protection Bureau's ability-to-repay rule, which sets the baseline for a Qualified Mortgage.

I am concerned that the Qualified Mortgage's 3 percent cap on points and fees will especially affect first-time home buyers and low- and moderate-income consumers, especially in places like my hometown of New York, which has some of the highest closing costs in home mortgages. It is problematic to me to include some specific closing cost charges in the cap, such as title insurance premiums from affiliated providers, escrow charges for future payment of tax and insurance, and low-level pricing adjustments which allow borrowers with not-so-perfect credit scores to qualify for affordable loans, and the double counting of loan officer compensation, which is unfair.

With respect to title charges, we must be careful not to treat title insurance companies differently under the QM rules based on their business affiliations. The home purchase and settlement process is complex and difficult for most home buyers. If a buyer chooses the one-stop-shopping option by selecting an affiliated title company, he or she ought to be able to exercise that option without the penalty of extra points on their mortgage.

To ensure that we have a thriving housing recovery that is far-reaching and sustainable, we need to make sure that we have a financial system that provides access to credit in underserved communities and affordable loans to low- and moderate-income households. Our financial regulations must, therefore, be balanced between the need to protect against excessive risk-taking and enabling a liquid, well-financed housing industry.

Consistent with this balanced approach, I support risk-retention rules as an important principle and risk-management tool in the securitization process. And risk retention would ensure that loan originators applied prudent underwriting standards at the critical initial stage of risk assessment.

Under Dodd-Frank, securities-based Qualified Residential Mortgage (QRM) loans would be exempt from risk-retention rules, as these loans would have been vetted as having gone through prudential underwriting standards.

The housing sector is vital to our economic recovery, and H.R. 1077 is an important step in ensuring that this sector remains vibrant and accessible to all niches of the population.

Chairwoman CAPITO. Thank you.

Mr. Duffy for 2 minutes.

Mr. DUFFY. First, I want to thank Chairwoman Capito for holding today's very important hearing, and I appreciate the panel coming in and sharing your views with us on our mortgage market.

I think everyone on this panel agrees that after the 2008 crisis, we have to have a review on what happened in regard to our underwriting standards with regard to our mortgages. I think it is fantastic that we have a bipartisan understanding that Dodd-Frank isn't perfect and that there is room to improve the law that was written a few years ago. I am hoping this can be one leading committee on bipartisan activity.

One of my concerns is specifically the civil liability that is imposed on banks in regard to assessing a borrower's ability-to-repay, specifically in regard to those banks that originate and retain their mortgages on their books. They assume the traditional credit risk of that loan, but then now they also have a civil liability on top of the traditional credit risk. I am interested in the panel's views on how that will impact the industry's willingness to write mortgages in this new environment.

Also, I have read most of the testimony, and a lot of you have talked about the safe harbor rule under QM, and I am interested in the panel's views on whether we can pierce—or an aggressive litigant can pierce that safe harbor rule and actually successfully litigate a positive outcome when our originators actually believe they were safely covered under the safe harbor rule.

Listen, I come from a rural part of the country. It is moderate and low income. I am concerned on how the ability-to-repay standard, as well as QM, is going to impact my constituents' ability to obtain mortgages as we move forward with these new rules. I look forward to the panel's testimony and our bipartisan work on this committee.

I yield back.

Chairwoman CAPITO. The gentleman yields back.

I now yield 3 minutes to the ranking member of the full Financial Services Committee, Ms. Waters from California.

Ms. WATERS. Thank you very much, Madam Chairwoman.

All of us on this committee know the 2008 financial crisis was a complicated event without a simple explanation, and I am sure there are differences of opinion on both sides of the aisle as to what led us into the greatest economic downturn since the Depression.

We can all agree on at least one thing: Mortgage lenders were extending loans to people who couldn't afford to pay them back. Underwriting standards went out the window as lenders raced to push as many people into complicated loan products as possible. Many borrowers who were eligible for prime rates received subprime loans from unscrupulous lenders that were compensated by yield spread premiums. The mortgage market wasn't working for its customers at all and many homeowners are still struggling with their lingering problems in the housing market.

In court documents released just last Friday, several employees of one of the Nation's largest mortgage servicers claimed that their managers encouraged them to pretend they had lost customer paperwork so the customers could be foreclosed upon. As it turns out, when the servicer doesn't own the loan it is servicing, it is cheaper to foreclose than to help a homeowner with a loan workout.

This misalignment of economic incentives is what the CFPB's ability-to-repay rule is all about. Rather than banning any type of loan product or feature, the Dodd-Frank Act empowered the Federal Reserve and the CFPB to go after lenders who recklessly trapped borrowers in loans they couldn't afford and provided consumers with additional rights to pursue compensation for faulty loan products. But Congress also realized it would be unfair to make lenders bear all of the risk these new rules present, so we worked with the industry to craft a set of standards which a mortgage could meet in order to be automatically exempted from the penalty set up to catch bad actors.

The CFPB has proposed a final rule on these so-called Qualified Mortgages, and I believe that rule has struck a very fair balance for the industry. The Qualified Mortgage rule incentivizes lenders to avoid complicated and risky loan structures with variable rates or features that allow borrowers to stay current while actually accruing more debt on their home, and it doesn't prevent them from doing so.

It encourages lenders to really look into a potential borrower's income documentation and compare that to the real payments the loan will require, not the tiny payments associated with a short-term teaser rate, but it doesn't force them to. And the Bureau has also made several adjustments to that rule addressing industry concerns, and I hope they will continue to work closely with the industry to strike the right balance of protection, specifically for rural lenders where credit availability is already a concern.

I believe that Director Cordray's establishment of the CFPB Office of Financial Institutions and Business Liaison will be very helpful to that effort.

I yield back.

Chairwoman CAPITO. Thank you.

Mr. Miller for 2 minutes.

Mr. MILLER. I want to thank the Chair for holding this important hearing today. We are starting to see a rebound in the housing market, and that is really important to the economic recovery of this country and for job creation. But we need to be cautious that Federal policies don't have a negative impact on that. And the CFPB's ability-to-repay rule governs lending for the foreseeable future for all of us, without a doubt.

But the rule contains Qualified Mortgage, called QM, and it is meant to protect consumers from subprime loans that are really predatory, but I have some real concerns with that. I have had a concern with the definition between subprime and predatory for years, and I am glad to see we are going to finally deal with it. But when you look at the concerns we have on that, the way it is written it could prevent creditworthy borrowers from being able to actually get a home and get a loan.

Some studies that have been released lately, one done by CoreLogic, says that about half of the mortgages that originated in 2010 could not be issued under this rule. The problem I have with it is that the mortgages in 2010 are performing very well. So if there is a problem with those loans, I think we need to look at them, but from what I am seeing, there doesn't appear to be a problem.

I have spoken with loan originators up and down the spectrum, from mortgage brokers to mortgage bankers to retail banks, and they all said basically the same thing: "We will not originate a non-Qualified Mortgage; there is too much liability." The Administration doesn't seem to see a problem with this, but the marketplace does notice a huge problem.

I support sound underwriting standards, but I am concerned the QM definition is basically too narrow and sometimes unclear. And there is an issue of a 3 percent point fee cap to determine someone's ability-to-repay a loan, and there are so many exclusions to that, it doesn't seem to make any sense. And the thing that I have problems with is you can't even drop that fee cap once you state what it is going to be in order to close a loan, even to the benefit of the buyer and the seller.

So we need to look at that issue and say, is it going to work, is it not going to work? But our housing market, as I said, is finally showing signs of life and I am concerned that what we are doing here could have a negative impact.

I yield back the balance of my time.

Chairwoman CAPITO. The gentleman yields back.

Mr. Ellison for 2 minutes.

Mr. ELLISON. Thank you. Thank you, Madam Chairwoman. Thank you, Madam Chairwoman and Mr. Ranking Member, for holding this important hearing.

I was intrigued by the title, "Examining How the Dodd-Frank Act Hampers Home Ownership." I don't know a lot, but I do know that homeowners paying fees completely separate from the actual cost of the service they receive is a damper on home ownership. Appraisal fees, title insurance, private mortgage insurance, all manner of inflated fees raise the cost of a mortgage by thousands of dollars.

I know that using language, or ethnic or religious affiliation to trick people into high-cost mortgages when they qualify for low-cost prime mortgages hampers home ownership. We have a lot of examples here of that. For example, Wells Fargo paid $175 million to settle accusations that it allegedly discriminated against African-American and Latino home buyers. An NAACP study found that African-American home buyers are 34 percent more likely to receive a subprime loan than White borrowers even when other factors are equal.

Of course, foreclosures don't help home ownership, either. We have had 4 million of them so far.

So when I think about the title of this hearing, and it seems to imply that Dodd-Frank is the problem with home ownership, I think that a whole lot of things that led up to the establishment of Dodd-Frank actually are the real problem with home ownership.

This isn't to say that we shouldn't look at how we can improve things and we shouldn't continue to refine the bill, but I do think that it is important to maintain some perspective on how we arrived at Dodd-Frank and what we are doing now, and I don't think that associating Dodd-Frank with being some barrier to home ownership is fair.

The global financial crisis cost this economy $16 trillion in wealth. The Qualified Mortgage and other elements of the Dodd-Frank Reform and Consumer Protection Act are not hampering home ownership. Dodd-Frank enables sustainable home ownership. We don't want somebody to get into a home that they can't keep. That is not promoting home ownership. That is putting somebody in a situation where they are set up to fail.

So I hope that despite today's title of this hearing, we can have some testimony that will actually show us how the Consumer Financial Protection Bureau is doing some good things and helping safeguard the American people's economic interest. Thank you.

Chairwoman CAPITO. Thank you.

Mr. Barr for 1 minute.

Mr. BARR. Thank you, Chairwoman Capito, for holding this very important hearing to examine the consequences of Dodd-Frank on home ownership.

A theme that I consistently hear from the community bankers in Kentucky's Sixth Congressional District is that they no longer have the discretion and flexibility to serve their communities in the ways that they know best. Whereas individual business judgment and institutional knowledge of the community should be considered strengths, and strengths that are encouraged, these bankers tell me that rather than focusing on their core business, they instead have to devote an increasing amount of time to playing catchup with regulations from Washington.

While each story is unique, the tale of the financial institution where personnel hiring in the compliance department dramatically outpaces hiring in the lending department is not unique. Some bankers have gone so far as to tell me that this new wave of regulations and lending rules in Dodd-Frank is leading them to seriously rethink their business model and whether they should get out of providing home mortgage services altogether.

I am confident that many in this room have heard these same concerns, and so I look forward to the opportunity presented by today's hearing to further explore Dodd-Frank, the CFPB rulemaking, the QM rule, and whether it truly strikes the proper balance between safety and soundness of our financial system and making sure creditworthy borrowers have access to the mortgage credit they need to purchase a home.

Chairwoman CAPITO. The gentleman's time has expired.

The gentlelady from New York for 2 minutes.

Mrs. MALONEY. I thank the chairlady and the ranking member and all of the panelists for being here. It is no secret that leading up to the financial crisis, mortgage lending was literally out of control, with prudent underwriting taking a back seat to profit-seeking.

The comment in New York was, if you can't afford to pay your rent, then go out and buy a home: no documents, no requirements, you can buy a home. And this hurt our economy, it hurt homeowners, it hurt our overall country, and it really alerted us to the need for greater standards and a minimum of safeguards for mortgage lending practices. That is what Dodd-Frank tried to accomplish, to show that we learned from our mistakes and that basic underwriting standards to prevent this from happening again were needed.

With the new QM rule, we will hopefully be able to assure borrowers that they are better protected from predatory lending practices. The debt-to-income ratio of 43 percent is one that the FHA has used for decades. I understand that the CFPB has granted an exception to that for community bankers to have their discretion with balloon loans to make appropriate loans that they feel are appropriate for that individual. But it does come forward with an overall standard, which I believe is necessary and that Dodd-Frank dictated.

We have to start somewhere. We can't go backwards. I compliment the CFPB on their hard work and for giving us a document to work from. And I look forward to the testimony of the witnesses and your reaction to the proposed rule that the CFPB has put forward. Thank you for your hard work. Thank you for being here.

Chairwoman CAPITO. Thank you.

Mr. Pittenger for 1 minute.

Mr. PITTENGER. Thank you, Chairwoman Capito, for calling this important meeting and for allowing me to make an opening statement.

We are here today to focus on the rules and regulations coming out of Dodd-Frank and out of these new policies that will affect home ownership across America, specifically regarding the ability-to-repay QM rule.

However well-intentioned, it will end up restricting mortgage credit, making it more difficult to serve a diverse and creditworthy population. The definition of QM, which covers only a segment of loan products and underwriting standards and serves only a segment of well-qualified and relatively easy to document borrowers, could undermine the housing recovery and threaten the redevelopment of a sound mortgage market.

The CFPB's QM rule has caused great concern among banks and credit unions, especially with the new exposure to litigation from borrowers not being able to repay the loan. During meetings back in the district, I have found the fears from banks, large and small, and credit unions that the regulators will view any loan outside the QM standards as a risky loan that will be used against the financial institutions as a safety and soundness issue.

With these new policies set to take effect in January of next year, my fear, as well as that of other Members, is that these new regulations will ripple throughout the economy and could lead to further anemic economic growth. It is my goal from this hearing that the CFPB hears the—

Chairwoman CAPITO. The gentleman's time has expired.

Mr. PITTENGER. —bipartisan calls of concern and addresses these issues. Thank you.

Chairwoman CAPITO. And last, but not least, Mr. Fitzpatrick for 1 minute.

Mr. FITZPATRICK. Thank you, Madam Chairwoman. And I appreciate the witnesses coming before the committee to discuss this really important issue.

I meet on a regular basis with REALTORS®, community banks, credit unions, and homebuilders in my district back home in Bucks and Montgomery Counties, Pennsylvania. We discuss ways to improve access to home ownership and to boost the housing market.

And while we all support the CFPB's efforts to ensure that consumers are able to repay their loans, I continue to hear concerns that the Qualified Mortgage rule discriminates against small lenders, minimizes consumer choice in lending, restricts access to credit, and makes providing credit much more costly. As a result, the QM rule may significantly cut down the number of mortgages being made, and many small lenders have indicated a reluctance to provide any mortgages at all under the rule.

This is a pretty tough economic market condition we find ourselves in. I believe Congress and the CFPB should instead be improving lending conditions so that individuals and families who have the ability-to-repay their loans have access to the affordable credit that they need. And so, we are all looking forward to the testimony here today.

And I appreciate the hearing, Madam Chairwoman. I yield back.

Chairwoman CAPITO. Thank you.

And that concludes our opening statements. I would like to yield to the gentleman from Kentucky, Mr. Barr, to introduce our first witness.

Mr. BARR. Thank you, Madam Chairwoman.

I am very proud today to welcome Commissioner Charles Vice to the Financial Services Committee. A resident of Winchester, Kentucky, Commissioner Vice has earned an outstanding reputation in the area of financial institution supervision, and we look forward to him sharing his expertise with the committee today.

Mr. Vice currently serves as the Commissioner of the Department of Financial Institutions for the Commonwealth of Kentucky, a position he was appointed to in August of 2008. In this role, Commissioner Vice has responsibility for the regulatory oversight of all State-chartered financial institutions in Kentucky, which includes examinations, licensing of financial professionals, registration of securities, and enforcement. It is a credit to Commissioner Vice that the financial institutions in my congressional district, which he interacts with on a regular basis, consistently tell me that he is knowledgeable, thoughtful, and fair in his role.

Commissioner Vice is also well-regarded by his peer supervisors. He serves in a national leadership capacity through the Conference of State Bank Supervisors, where he has been a member of the Executive Committee. Commissioner Vice formerly served as treasurer and chairman-elect of the CSBS board, and in May 2013, he officially became chairman of the governing board.

In addition to his service on a number of supervisory boards and committees aimed at improving examinations of financial institutions, Commissioner Vice previously worked for 18 years as an employee of the FDIC. During his tenure with the FDIC, Commissioner Vice served in the Lexington, Kentucky, field office, where he was the office's expert on subprime lending and capital markets. In recognition of his outstanding work, he received the FDIC Chicago Region employee of the year award in 2007.

And on a personal note, I just want to thank Commissioner Vice for his courtesy in being available to me and my staff, for answering our questions, and for sharing his considerable expertise and insights with us. I am honored to welcome Commissioner Vice to the committee, and we look forward him sharing his expertise on the impact of Dodd-Frank on home ownership.

Chairwoman CAPITO. Thank you.

Welcome, Commissioner Vice. You are recognized for 5 minutes.

And I would ask all the witnesses to please pull the microphones close to them, and make sure they are on, because sometimes it is difficult to hear, and we want to hear every single word.

So, Commissioner Vice, you are recognized for 5 minutes.

STATEMENT OF CHARLES A. VICE, COMMISSIONER, KENTUCKY DEPARTMENT OF FINANCIAL INSTITUTIONS, ON BEHALF OF THE CONFERENCE OF STATE BANK SUPERVISORS (CSBS)

Mr. VICE. Good morning, Chairwoman Capito, Ranking Member Meeks, and members of the subcommittee. Thank you, Congressman Barr, for your service to the Commonwealth of Kentucky and for your kind introduction today.

My name is Charles Vice, and I am the commissioner for the Kentucky Department of Financial Institutions. I am also the chairman of the Conference of State Bank Supervisors. And I appreciate the opportunity to testify today.

I have been a financial regulator, first with the FDIC, and now with the Commonwealth of Kentucky, for more than 20 years. During that time, I have observed a troubling trend. Federal regulators and policymakers seem to be taking a blanket approach to supervision, applying statutes and regulations to all banks regardless of size, location, ownership structure, complexity, or lending activities. This concerns me.

While today's hearing focuses on the ability-to-pay rule on the Qualified Mortgage, the broader issue for State supervisors is a one-size-fits-all approach to supervision and regulation. State regulators are dedicated to understanding the impact of the current regulatory environment on community banks. CSBS has established a Community Banking Task Force to explore these issues. Additionally, CSBS is partnering with the Federal Reserve System to host an upcoming community bank research conference.

State regulators have found that regulation and supervision needs to be more tailored to how community banks lend. Policymakers should not hinder portfolio lending; instead, they should ensure community banks are able to positively impact local and national economic conditions.

As a basic tenet of responsible underwriting, I believe lenders should determine a borrower's ability-to-repay a loan; however, community banks that hold loans in portfolio are motivated to ensure the borrower can make their mortgage payment. As such, lenders that retain the full risk of a borrower's default by community banks that retain mortgage loans in their portfolio should be presumed to have determined a borrower's ability-to-repay.

The CFPB has shown initiative by recognizing the portfolio lending business model. The small creditor QM creates a framework that supports retention of mortgages in portfolio by community banks. This right-sizing of regulation appropriately accounts for differences in community bank business model. Congress and Federal regulators should use the small creditor QM as an example for developing laws and regulations.

The treatment of balloon loans is one case where a one-size-fits-all approach falls short. Under the Dodd-Frank Act, balloon loans would only qualify for QM status if they originated in a rural or underserved area. When used responsibly, balloon loans are a useful source of credit for borrowers in all areas. This provision effectively limits a bank's flexibility to tailor products to the credit needs of the community. As a regulator, the banks under my purview and the consumers they serve benefit from having more products at their disposal. The CFPB has extended the timeframe before the balloon loan restriction takes place, potentially offering Congress the opportunity to act on this issue.

Congress should amend the statute to grant QM status to all mortgage loans held in portfolio by community banks. This is a portfolio lending issue, not a rule or underserved issue.

As a more immediate solution, and absent a legislative change, CSBS recommends a petition process to address inconsistencies for rule designations. The CFPB has the challenging task of providing an appropriate definition of rule. Unfortunately, the CFPB's approach has some illogical results. This is inevitable when local communities are defined by a formula developed in Washington, D.C. Therefore, the CFPB should adopt a petition process for interested parties to seek rural status for counties, a step that is within the CFPB's current authorities.

State regulators stand ready to work with Members of Congress and our Federal counterparts to develop and implement a supervisory framework that recognizes the importance of our unique dual banking system.

Thank you for the opportunity to testify today on this important topic.

[The prepared statement of Commissioner Vice can be found on page 109 of the appendix.]

Chairwoman CAPITO. Thank you, Commissioner.

Next, I would like to recognize my fellow West Virginian, Mr. James C. Gardill, who is chairman of the board of WesBanco, Incorporated. He is testifying on behalf of the American Bankers Association. He has a distinguished career as a banker and an attorney in the northern panhandle of West Virginia.

He and I have the distinction of being from Glen Dale, West Virginia, which we share that distinction with being the birthplace of Brad Paisley and the home of Lady Gaga's grandparents.

With that, I would like to thank Jim for coming today, and I look forward to his 5-minute presentation. Thank you.

STATEMENT OF JAMES GARDILL, CHAIRMAN OF THE BOARD, WESBANCO, ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION (ABA)

Mr. GARDILL. Chairwoman Capito, Ranking Member Meeks, my name is James Gardill, and I am chairman of the board of WesBanco, a $6.1 billion bank holding company headquartered in Wheeling, West Virginia. We are active mortgage lenders with a $1.3 billion mortgage portfolio. I appreciate the opportunity to be here to represent the ABA regarding the new ability-to-repay and Qualified Mortgage rules.

The mortgage market generates a substantial portion of the GDP and touches the lives of nearly every American household. The new ability-to-repay and Qualified Mortgage rules represent a fundamental change in this market. As such, it is critical that these rules make sense and do not end up hurting creditworthy Americans who strive to own a home.

Unfortunately, the ability-to-repay and QM rule, however well-intentioned, will restrict mortgage credit, making it more difficult to serve a diverse and creditworthy population.

Under the ability-to-repay rule, underwriters must consider a borrower's ability-to-repay a mortgage loan. Qualified mortgages are designed to offer a safe harbor within which loans are assumed to meet the ability-to-repay requirement. However, the QM rules create a narrowly defined box that consumers must fit in to qualify for a QM-covered loan. Banks are not likely to venture outside the bounds of the QM safe harbors because of the heightened penalties and liabilities applicable under the ability-to-repay rule.

Since banks will make few, if any, loans outside of QM standards, many American families who are creditworthy but do not fit inside the QM box will be denied access to credit. In the short run, this could undermine the housing recovery.

More fundamentally, this also likely means that less affluent communities may not be given the support they need to thrive. These rules may leave many communities largely underserved in the mortgage space.

In particular, I am concerned that our bank will be unable to continue several loan programs targeting low- and moderate-income borrowers and neighborhoods. Our CRA Freedom Series forums and a charitable plan we administer designed to promote home ownership for families, our Laughlin plan, provides financial aid to families who would otherwise not be able to own a home, in the form of interest-free loans and insurance. These loans would likely not qualify for QM status, with some failing to meet the ability-to-repay requirements, meaning we would not be able to make them at all.

Even if banks choose to make only loans that fit within QM, they still face a number of risks. Higher-interest-rate loans still carry both higher credit risk and liability risk under QM's rebuttable presumption. This means banks will be hesitant to offer them, instead serving only the best qualified borrowers. The end result of this will be less credit available to some individuals and communities, creating conflict with fair lending rules and the goals of the Community Reinvestment Act.

The rulemaking has left banks little time to comply with the QM regulations, despite the wide-ranging market implications and the tremendous amount of work which banks must undertake to comply with these rules. Currently, these and five other mortgage rules are scheduled to go into effect in January of 2014. Between now and then, banks must fully review all of the final rules, implement new systems, processes and forms, train staff, adapt vendor systems, and test these changes for quality assurance before bringing them online.

Some institutions may simply stop all mortgage lending for some time because the consequences are too great if the implementation is not done correctly. I recently learned of a vendor that will not have the majority of its updates out until November 22nd, leaving its customers 7 weeks to customize, update, and train staff.

These rules must be revised so that they help the economy and at the same time ensure that the largest number of creditworthy borrowers have access to safe, quality loan products. In order to do this, we need to extend the existing deadlines, as well as address these outstanding issues.

Thank you very much. I am happy to answer any questions that you may have.

[The prepared statement of Mr. Gardill can be found on page 63 of the appendix.]

Chairwoman CAPITO. Our next witness is Mr. Jerry Reed, chief lending officer, Alaska USA Federal Credit Union, on behalf of the Credit Union National Association. Welcome.

STATEMENT OF JERRY REED, CHIEF LENDING OFFICER, ALASKA USA FEDERAL CREDIT UNION, ON BEHALF OF THE CREDIT UNION NATIONAL ASSOCIATION (CUNA)

Mr. REED. Chairwoman Capito, Ranking Member Meeks, thank you for the opportunity to testify at today's hearing. I am Jerry Reed, chief lending officer of Alaska USA Federal Credit Union, which is based in Anchorage, Alaska. I am here today representing the Credit Union National Association. We greatly appreciate the attention this subcommittee has given to the Qualified Mortgage regulation issued by the CFPB. We also appreciate the consideration the Bureau has given credit unions in the rulemaking process. However, we have significant concerns with how the rule may be implemented.

My written testimony describes our concerns in detail, and I want to discuss a few of them with you today: first, I want to explain why all credit unions should be fully exempted from the QM rule; second, I want to discuss the impact the rule will have on the secondary market; third, I want to discuss how our regulators may view non-QM loans that credit unions may wish to add to their portfolios in the future; and fourth, I want to discuss our concern that QM may result in unintended disparate impact on the ability of otherwise creditworthy borrowers to achieve the American dream.

Recent revisions provide QM status to loans originated by institutions of $2 billion or less in assets that originate 500 or fewer first lien mortgages. We believe this is a good start, but unfortunately it only covers about a quarter of credit union lending. Since loan losses are so minimal across all sizes of credit unions, it is clear the cooperative structure and purpose of credit unions, not their size, leads to quality loan decisions for the borrower and their ability and willingness to repay.

Since the onset of the financial crisis, annual losses on the credit union first mortgages have averaged only 0.29 percent, compared to 1.13 percent at banks.

The structure of credit unions merits the exemption, because we are operationally conservative and already have been applying ability-to-repay standards for years in the normal course of business to minimize loan losses. Moreover, the Bureau has clear statutory authority to go further in exempting credit unions and deeming all credit union mortgages as QM loans.

Given the recent announcement by the FHFA that Fannie Mae and Freddie Mac will not be able to purchase certain non-QM loans, credit unions are concerned about the long-term effect this rule and its application will have on the secondary market and what that means for credit unions and their members.

We ask the committee to ensure that credit unions have a functioning secondary market to sell loans, even if they do not meet the QM definition, if they otherwise meet secondary market standards. Being unable to sell non-QM loans to the secondary market will make the management of assets at a credit union difficult.

Prudent interest rate risk management requires being able to sell long-term fixed rate loans into an efficiently functioning secondary market. It is paramount that Congress and the Bureau work closely with prudential regulators to ensure that this instrument of consumer protection does not become an instrument of prudential regulation.

Likewise, we have significant concerns that examiners will severely restrict the ability of credit unions to keep non-QM loans in their portfolio after the rule goes into effect. As well, the possibility exists that examiners will determine that non-QM mortgages are a safety and soundness concern, resulting in a downgrade in credit unions and their associate camel ratings.

As the economy recovers, the credit union model continues to serve credit union members well, but the QM rule has the potential to fundamentally alter that relationship. In fact, had this rule been in effect during the crisis, it is very likely that as the economy worsened, NCUA examiners would have increasingly frowned on non-QM loans, making it that much more difficult for credit unions to continue to lend when other providers did not.

Director Cordray has indicated his support of non-QM loans made by credit unions. It is essential that Congress direct other regulators to follow the lead of the Bureau in this matter so that non-QM loans and the availability of loans to creditworthy borrowers should be encouraged and not viewed negatively by examiners.

As I have pointed out, the QM rule forces individuals into a one-size-fits-all box. Equally, this could result in the unintended consequence of disparate impact in residential mortgage lending. It would restrict the ability to sell those mortgages to the secondary market and hold them in portfolio. This would ultimately exclude borrowers with perfectly good abilities to repay, but who do not meet the specifics of the QM rule. This would make it more difficult for credit unions to fulfill their purpose of providing credit to all who could benefit from it and are able to repay it.

Thank you again for the opportunity to testify at today's very important hearing.

[The prepared statement of Mr. Reed can be found on page 75 of the appendix.]

Chairwoman CAPITO. Thank you, Mr. Reed. And, boy, you have really brought them to their feet out there.

Our next witness is Ms. Debra Still, no stranger to the committee. Welcome back.

Ms. STILL. Thank you.

Chairwoman CAPITO. She is the chairwoman of the Mortgage Bankers Association.

Welcome.

STATEMENT OF DEBRA W. STILL, CMB, CHAIRMAN, MORTGAGE BANKERS ASSOCIATION (MBA)

Ms. STILL. Thank you very much, Chairwoman Capito and Ranking Member Meeks.

Since I last testified before your committee, the CFPB has finalized the ability-to-repay rule, including the definition of a Qualified Mortgage. Lenders are now fully focused on understanding and implementing this new rule by its effective date of January of next year. Of all of the Dodd-Frank rules, QM will have the single-most significant impact on consumer access to credit and a vibrant competitive marketplace.

The industry applauds the CFPB for getting a lot right, using a deliberative and inclusive approach. Most notably, the CFPB established a safe harbor for most QM loans and a temporary QM, both critical provisions for borrowers. But there is still serious concern that certain aspects of the rule will be prohibitive to otherwise qualified consumers.

QM takes effect at a time when credit is already overly tight and underwriting standards are well above industry norms. In the current form, this rule could cause unintentional harm to the very consumers it was designed to protect and make lenders even more cautious than they are today.

In the foreseeable future, MBA believes that lending will be substantially limited to loans that meet the definition of a Qualified Mortgage with a safe harbor provision. QM loans with a rebuttable presumption and non-QM loans will have little market liquidity and, if available at all, will be more costly for borrowers.

The element with the greatest potential for unintended consequences is the 3 percent cap on points and fees. The points and fees test is a threshold requirement for all QM loans. The calculation is highly complex and is based on criteria unrelated to credit quality, and penalizes both affiliate and wholesale lenders.

This inconsistent treatment impairs a consumer's ability to shop and their choice in settlement service providers. Any negative impact will be on smaller loan amounts and fall most heavily on low-to moderate-income and first-time home buyers.

I want to thank Congressman Huizenga for introducing H.R. 1077, the Consumer Mortgage Choice Act, and also the many members of this subcommittee who have given this legislation the broad bipartisan support it currently enjoys. The ability-to-repay rule must be centered on consistent consumer protection regardless of business model. H.R. 1077 will fix the points and fees calculation, leveling the playing field. By passing the bill before January 2014, Congress will ensure a vibrant, competitive marketplace for consumers.

For the same reason, we also suggest that an additional way to reduce QM's impact would be to raise the small loan limit to $200,000, and increase the points and fees limit to 4 percent, and up to 8 percent for very small balance loans.

The QM rule is so vital it is imperative that it be aligned with other Federal regulations. Lenders are seeking clear guidance on reconciling QM with other compliance obligations. Specifically, HUD's disparate impact rule makes lenders liable under the Fair Housing Act for mortgage lending practices if they have a disproportionate effect on protected classes of individuals, even if the practice is neutral and nondiscriminatory. If a lender limits its listing to QM loans only, the lender may face exposure under the disparate impact rule. Lenders must have more certainty that their decisions with respect to QM will not place them in jeopardy.

Of equal significance is the need for clear alignment between QM and the definition of a Qualified Residential Mortgage within the pending risk retention rule. MBA believes that it is essential that QRM equals QM, particularly as it relates to the elimination of prohibitive downpayment requirements in QRM. Any variation between these two rules will increase the cost of credit, discourage private capital, and add to the complexity of mortgage finance for industry participants and consumers alike.

Chairwoman Capito, I want to thank you and your colleagues for your continued focus on this highly complex QM rule. We all share the same goal: to strike the right balance between consumer protection and access to credit. If not appropriately modified, this well-intentioned rule may fail consumers in the most fundamental way.

Access to safe and affordable credit is vital to the future growth of home ownership in America. In the months ahead, we urge you to encourage the CFPB to exercise its authority to make change and we ask for your support for speedy passage of H.R. 1077.

Thank you.

[The prepared statement of Ms. Still can be found on page 87 of the appendix.]

Chairwoman CAPITO. Thank you.

Our next witness is Mr. Gary Thomas, president of the National Association of REALTORS®. Welcome.

STATEMENT OF GARY THOMAS, PRESIDENT, NATIONAL ASSOCIATION OF REALTORS® (NAR)

Mr. THOMAS. Thank you. Madam Chairwoman, Ranking Member Meeks, and members of the subcommittee, on behalf of the 1 million members of the National Association of REALTORS®, whose members practice in all areas of residential and commercial real estate, thank you for the opportunity to participate in this hearing.

I am Gary Thomas, president of the National Association of REALTORS®, from Orange County, California, and I have more than 35 years experience in the real estate business. I am the broker-owner of Evergreen Realty in Villa Park, California.

The Dodd-Frank Wall Street Reform Act established the Qualified Mortgage, or QM, as a primary means for mortgage lenders to satisfy its ability-to-repay requirements. However, Dodd-Frank also provides that a QM may not have points and fees in excess of 3 percent of the loan amount.

As currently defined by Dodd-Frank and the Consumer Financial Protection Bureau's final regulation to implement the ability-to-repay requirements, points and fees include fees paid to affiliated title companies, amounts of homeowners insurance held in escrow, loan level price adjustments, and payments by lenders in wholesale transactions. Because of this problematic definition, many loans made by affiliates, particularly those made to low- and moderate-income borrowers, would not qualify as QMs. Consequently, these loans would be unlikely to be made or would only be available at higher rates due to the heightened liability risk. Consumers would lose the ability to choose to take advantage of convenience in market efficiencies offered by one-stop shopping.

To correct unfairness in the fees and points calculation, the National Association of REALTORS® supports H.R. 1077, the Consumer Mortgage Choice Act. The bill has been introduced by Representatives Huizenga, Bachus, Royce, Stivers, Scott, Meeks, Clay, and Peters. Similar legislation has been introduced by Senators Manchin and Johanns in the Senate.

The legislation solves a problematic definition of points and fees in several distinct ways. First, it removes affiliated title insurance charges from the calculation of fees and points. The title industry is regulated at the State level and is competitive. It does not make sense to discriminate against affiliates on the basis of these fees. To do so only reduces competition and choice in providers of title services, to the detriment of consumers.

Furthermore, owners of affiliated businesses can earn no more than a proportionate return on their investment under the Real Estate Settlement Procedures Act (RESPA). RESPA also prohibits referral fees or any compensation at all for the referral of settlement services. As a result, there is no steering incentive possible for individual settlement service providers such as mortgage brokers, loan officers, or real estate professionals.

Consumers repeatedly have said that they want the convenience of one-stop shopping since buying a home is complicated, and for most buyers, they will only do it a couple of times in their lifetime. This legislation will continue to allow ease and accessibility offered through one-stop shopping. NAR believes legislative language is necessary to ensure that efficient business models are not unfairly discriminated against in the calculation of fees and points.

Second, the legislation removes the calculation of fees and points Fannie Mae and Freddie Mac loan level price adjustments. This money is not retained by the lender. These adjustments are essentially risk-based pricing established by the GSEs and can sometimes exceed 3 points in and of themselves. Including these loan level price adjustments would limit access to affordable mortgage credit to many borrowers or force borrowers into more costly FHA or non-QM loans unnecessarily.

Finally, the bill removes from the calculation of fees and points escrows held for taxes and insurance. The tax portion is a clarification of imprecise language in Dodd-Frank. In the case of insurance, these escrows are held to pay homeowners insurance and can be a large amount. They are not retained and cannot be retained by the lender since RESPA requires excess escrows to be refunded.

Once again, NAR supports a legislative fix because it is the most certain way to avoid future confusion and legal risk.

In conclusion, NAR believes H.R. 1077 is essential to maintain competition and consumer choice in mortgage origination. Without this legislation, research shows that up to one-half of the loans currently being originated would likely not be eligible for the QM safe harbor and would likely not be made by affiliated lenders. Instead, if loans are made at all, they would be concentrated among the largest retail lenders, whose business models are protected from the points and fees definition discrimination.

It is for these reasons that NAR urges Congress to pass H.R. 1077 well before the ability-to-repay provisions take effect in January 2014, since lenders are likely to begin adjusting their systems in the fall of 2013.

Thank you for the opportunity to share our thoughts. We look forward to working with Congress and the Administration on efforts to address the challenges still facing the Nation's housing markets.

[The prepared statement of Mr. Thomas can be found on page 104 of the appendix.]

Chairwoman CAPITO. Thank you.

Our final witness is Mr. Michael D. Calhoun, president of the Center for Responsible Lending.

Welcome.

STATEMENT OF MICHAEL D. CALHOUN, PRESIDENT, CENTER FOR RESPONSIBLE LENDING (CRL)

Mr. CALHOUN. Thank you, Chairwoman Capito, Ranking Member Meeks, and members of the subcommittee for this opportunity to testify today.

It is important to remember that unsustainable mortgages were at the heart of the financial crisis. Large fees were paid for originating unnecessarily risky mortgages. For example, a no-doc loan or an exploding ARM loan would pay twice as much in fees as a 30-year fixed-rate loan to the exact same borrower, and thus it is no surprise that those exotic products came to dominate the market. The response of the ability-to-repay provisions requires that lenders make loans based on the borrower's capacity to repay, and we are all better off for that.

In my testimony, I am going to emphasize three points. First, excluding broker fees made by creditors from the points and fees tests would reinstate these incentives for risky lending. Second, lenders should not be rewarded with a competitive advantage by encouraging and steering borrowers to use their own service providers. And finally, existing exceptions to the QM points and fee tests already provide ample space for broad lending.

On the first issue, one of Dodd-Frank's central mortgage reforms was including payments made by creditors to brokers in the points and fees. This followed the practice that had been tried successfully in a number of States around the country for many years. It is based on common sense and reflects the experience of the financial crisis.

First, broker payments are generally included, and should be included in points and fees. The broker is supposed to be providing origination services that reduce the lender's costs that they would otherwise charge for. Brokers can be paid directly by the borrower. Everyone agrees those fees can be included. As an alternative, brokers can be paid by the creditor, and those are intended to be a direct substitute for the borrower fee and should likewise be included.

Most important, these are essential to prevent steering. A broker could provide only high-priced loans with very high broker fees, and those would not violate the other anti-steering provisions of Dodd-Frank. They would, though, provide a powerful incentive to steer borrowers to those loans. That steering is bad for all home buyers, and is particularly bad for families of color. The National Council of La Raza, NAACP, the Leadership Conference on Civil Rights, and other civil rights groups oppose H.R. 1077, which would bring back this tool of discrimination.

On the second issue, affiliated services have been counted in points and fees under Federal law for nearly 2 decades, and it is especially important for title insurance. Title insurance is negotiated between the title insurer and a third-party agent, even though it is the consumer paying the fee. Not surprisingly, out of every dollar of title insurance, which can be $1,000 to $2,000 on a mid-sized loan, only 10 cents goes to actually paying claims; 75 cents of that dollar gets paid out as commissions. When affiliated title services are used, the lender captures part of the title charge, increasing its revenue on the loan. This should not be a competitive advantage and windfall for that lender, but rather should be reflected in lower fees elsewhere in the loan.

Third, the points and fees test, and this is very important, has many provisions that already permit loans fees meet its test. First, third-party fees are not included. Legal fees, filing fees, insurance fees, and other items are explicitly excluded. Second, on top of the fee amounts, an additional 2 discount points can be charged and not counted in the points and fees test. Third, for smaller loans, they have higher fee thresholds, for example 5 points for a $60,000 loan and even 8 points for very small loans. Finally, lenders can recoup their costs by including them in the interest rate instead of charging upfront fees. This is what lenders have historically done.

Fannie and Freddie report today, as of last week, that average lender fees are less than 1 point—1 point—and this aligns the interest of the borrower and the lender with both profiting from performance of the loan rather than from large feels at closing.

In summary, H.R. 1077 as it is currently drafted would produce steering, higher fees for borrowers, and more concentration in the mortgage market as larger lenders are most able to take advantage of its provisions.

Thank you again for the opportunity to testify, and I look forward to your questions.

[The prepared statement of Mr. Calhoun can be found on page 44 of the appendix.]

Chairwoman CAPITO. Thank you.

That concludes the testimony of our panel, and I will begin with questioning for 5 minutes. I want to thank you all before I begin that.

Mr. Gardill, we have talked about the Laughlin program, which is the charitable program. Do you know approximately how many families have been assisted by that program in the life—I believe it began in 1951?

Mr. GARDILL. Several hundred, Chairwoman Capito. We currently have 100, roughly 100 active borrowers, but several hundred over the last several decades.

Chairwoman CAPITO. Right.

Mr. GARDILL. Probably over 1,000 at this point.

Chairwoman CAPITO. Right. You don't believe that you can continue this charitable program that really is the only way for these families to get into a home under your guidance. It has been very successful, I understand. You obviously have some underwriting standards that you put into effect that don't fit into the QM box. Is that the gist?

Mr. GARDILL. That is correct. We look at the individual credit, so we have flexibility in designing that opportunity for that customer. It applies to heads of households and single parents with two or more children. We don't fit in the box that they have designed.

Chairwoman CAPITO. So you would discontinue writing those loans, then?

Mr. GARDILL. We would have to severely reduce it, maybe even have to discontinue it entirely.

Chairwoman CAPITO. Okay. There has been a study looking at the mortgages of 2010 that only 52 percent of those mortgages that were made in 2010 would actually fit into the definition for the safest loans under the QM rule.

As a banker in West Virginia, what happens to the other 48 percent of those mortgages, in your opinion, once this rule goes into effect.

Mr. GARDILL. They probably won't be made.

Chairwoman CAPITO. Will they be made at all by any other sort of institutions or any online lenders or—

Mr. GARDILL. I think the market is going to have to settle in. The problem is that period is going to create a severe restriction in lending. And it is going to hurt the most vulnerable the worst, and that will be the low to moderate income in the rural areas. We are in both large metropolitan areas and in rural areas and we see that impacting.

Last year, about 38 percent of our loans were sold in the secondary market. So we originated the rest of those in portfolio. As a community-based lender, we lend to our communities and support our communities. We can't fit everybody within the box that has been created.

Chairwoman CAPITO. Great. Thank you.

Commissioner Vice, you mentioned in your testimony—or it was mentioned actually by several folks—that if somebody does write a non-QM loan, what effect as a regulator will that have on your evaluation of that institution's safety and soundness? I think you mentioned a little bit in your statement. How are you going to be able to evaluate those loans, if in fact they are actually written, which is dubious at this point?

Mr. VICE. That is one thing the regulatory entities would have to determine, how to treat these going forward. First, there would probably have to be some kind of identification piece to it, some kind of monitoring piece to it.

The one thing I would hope is that it would not be an automatic detraction for an examiner going in and looking at a portfolio. Again, it should be on an individualized lending basis and the loan should be looked at and graded on its credit quality. And I would hope that all the Federal regulators and my fellow State regulators would not see a non-QM loan to be a negative or to hold that against the bank. Again, it needs to be looked at on an individual basis, and the credit quality of that individual loan has to be assessed.

Chairwoman CAPITO. Do you think there should be an exception from the ability-to-repay standards for loans that are held on portfolio?

Mr. VICE. Yes, yes. If a small community bank does originate a loan and hold it in their portfolio, we believe that that should receive QM status in and of itself, simply because it is being held in portfolio.

Chairwoman CAPITO. All right.

Mr. Reed, your State is very rural and much like our State, but you are probably a billion times bigger in land mass, and you rely on relationships to be able to help your constituents. With the new definitions of “rural,” and some of the one-size-fits-all definitions and ability-to-repay, what impact is that going to have on a State such as yours?

Mr. REED. Yes, the majority of our State is rural. You can fit three sizes of the State of Texas and the State of Alaska. So that kind of gives you an idea. A lot of that population is dispersed throughout that State in what we call the bush. And it is absolutely going to impact us.

I have to agree with Mr. Vice, that is one of the reasons that we are seeking an exemption. It is going to impact us significantly and our membership.

Chairwoman CAPITO. Thank you.

Mr. Meeks?

Mr. MEEKS. Thank you, Madam Chairwoman.

Let me go to Mr. Calhoun first. Clearly, no-doc loans, when you do no-doc loans you are saying that you are not looking at a person’s ability to pay, whether they are creditworthy, et cetera, and just passing it on. And it seems to me that one of the biggest issues that we were confronted with in this crisis is that there was no risk retention by many of the banks; they would just no-doc, bundle them, sell them, get rid of them. Some would steer people, but steer people basically, as Mr. Ellison indicated, some by race, et cetera, not treating people equitably who would go to a subprime loan and who would get a prime loan, et cetera. So no one agrees with steering, et cetera.

But are we talking about creating a situation where individuals who have less than perfect credit—and that is what I am concerned about—individuals now who have less than perfect credit, should they not have the opportunity to own a home? And what opportunity will be, what doors will be closed to them? Because I can tell you that, at least in the community that I was raised in, there were a lot of individuals, if you document their employment and you document their income, that they paid their mortgage, but they did pay some other bills late, so they didn’t have perfect credit.

And so, I am concerned about those individuals getting locked out of this market and trying to figure out how they can be included so that they can enjoy what has been—because I still believe home ownership is the American dream, it is still the largest investment that most Americans will make in their lifetime, and it improves family and quality of life.

Let me just ask this. For example—and one of the reasons I look at H.R. 1077, is it does call for loan-level price adjustments, so that individuals can qualify for a QM if they put up some upfront fees so that they will qualify, then they can go on. Now, they understand they made a mistake with some of their credit levels, so therefore they have to put these upfront fees. Had they not, then they wouldn’t have had to. So tell me how can we make sure that those individuals are included so they can still have the opportunity to purchase and own a home?

Mr. CALHOUN. The Center for Responsible Lending strongly supports broad lending activities. Our parent organization, that has been its mission for the last 35 years, is how do you expand the boundaries of home ownership opportunities.

I think a really important distinction, and I think there has been confusion on this today, is the QM rule—and there has been reference to the CoreLogic report, which included a provision that any loan eligible for insurance or purchase by any of the government agencies—FHA, VA, Rural Housing, the GSEs—is a QM loan. And as the CoreLogic report notes, when that is done, 95 percent of those loans qualify with no restructuring at all.

So first, I want to clear up—and we have supported making that provision permanent. They have made it, I think, for the next 7 years. We think the CFPB should make that permanent. But at least for that time period, the box is much bigger than has been talked about here. So, for example, for FHA, GSEs, that is credit scores in the 500s, that is DTI, debt to income, up to 50 percent, that is 50 percent of gross income before your taxes are paid, not a lot of left money there. Most people are criticizing FHA as being too loose with lending, not too tight.

So we support a broad box, but I think when you look hard at the particulars of this rule, it created a broad box.

Mr. MEEKS. Let me just ask Ms. Still to respond to that.

Ms. STILL. Yes, I think certainly the temporary QM that the CFPB provided for will be helpful in the short run. But you can't just look at the credit quality. You have to look at the fees and points test, which will have a disparate impact on smaller loan amounts, which will hurt middle-class home buyers, first-time home buyers, and protected classes. So I think that is something that H.R. 1077 would address and fix.

You also have to look at the notion of an APOR comparison and what that will do to certain consumers, and it will also disproportionately impact the first-time home buyer. And so with those two tests, you are going to not be able to take otherwise qualified borrowers and make a loan for them. You will either end up with a non-QM loan, in which there will be little liquidity for that product, or you will make a rebuttable presumption loan, which if there is a secondary market for that, it will be much smaller and it will be more costly.

Chairwoman CAPITO. The gentlemen's time has expired.

Mr. Duffy?

Mr. DUFFY. Thank you, Madam Chairwoman.

I think we find ourselves in another unique situation where bureaucrats in Washington know far better how to run our community banks and our credit unions than our community banks and our credit unions do. And it concerns a lot of us up here, especially those of us, again, from small communities who have lower-income and more moderate-income individuals. And when I look at the ability-to-repay rule, and the QM standard, if you are wealthy and have great credit this works fantastic for you. But if you are from a lot of our districts, this is tough.

As Mr. Meeks said, the American dream oftentimes is buying your own house. Home ownership is associated with the American dream, and so many more Americans aren't going to be able to access that dream because of these rules.

Mr. Gardill, you indicated that through your analysis, 50 percent of the loans that were written would not meet the QM standard. Is that correct?

Mr. GARDILL. It might be a little bit higher than that, Congressman Duffy.

Mr. DUFFY. So in regard to the 50 percent that don't meet the QM standard in your analysis, those folks who don't fall under QM, are they still creditworthy?

Mr. GARDILL. They are. We make loans to them every day. One of our problems, which I think Congressman Meeks spoke to, is that those with less than perfect credit, we have designed programs to meet their needs in our communities. This applies to banks regardless of size. And our hands are being tied, we are going to be restricted in what we can do. Our freedom series is designed for just that purpose. We would loan up to 97 percent loan to value, but we structured the loans to meet their opportunities. We are not going to be able to do that under these rules.

Mr. DUFFY. And how well did those loans perform, Mr. Gardill? And, Ms. Still, if you want to answer that as well?

Mr. GARDILL. The flexibility that we have to design those, they have worked very well. We actually received the FDIC Chairman's Award in 2011 for that program.

Mr. DUFFY. Ms. Still?

Ms. STILL. I would like to make one observation. Whether my colleagues point out the problems with rural communities or community banks or credit unions or portfolio lenders, the MBA represents all business models, all constituents of real estate finance, and our concern is that this rule—we have to get this rule right and it has to be centered on consumers. And any consumer with the same interest rate, points, and fees should be treated equally.

So while the problems that we are talking about and the request for exemption are relevant because the rules are not right yet, we need to get the rule right for every business model—and so that is just one thing I wanted to point out—rather than a very complex rule where a borrower can't shop anymore because they don't know which business model will treat them more favorably under access.

To answer your question, though, one of our concerns is now that the FHFA has chosen not to allow Fannie and Fannie to buy a non-QM loan, a loan that we would sell today based on acceptable credit quality to the GSEs, if it did not meet 3 point rule would now not be eligible to be sold. And so, we have mitigated the secondary market for otherwise qualified borrowers and that is a concern.

Mr. DUFFY. Banks and credit unions are pretty good at pricing risk. And is it fair to say there is a new risk with the ability-to-pay rule in that you have new liability, and with that new liability is new risk, and isn't it fair to say that we are going to have increased prices to accommodate that risk?

Ms. STILL. There will be a base price for a QM with a safe harbor, then we will have a price for a QM with a rebuttable presumption. We may have a price for a QM with using Appendix Q, and then we will definitely have an escalated price for a non-QM. So, we now have four classifications of risk-based pricing.

Mr. DUFFY. Mr. Calhoun, you had talked about a lot of these outrageous products that were offered. And I agree with you, they were outrageous, people weren't treated fairly, and it was part of the cause of the crisis. We are on the same page. But weren't a lot of those no-doc loans, weren't they all floated? Those loans weren't actually kept on the books of the originators, were they?

Mr. CALHOUN. It was a combination. And let me be clear, I think people do share similar goals here in getting this rule, it is important and hard. But many of those loans we are working right now with a loan program done by a community bank in New York that did thousands of loans and they are having about a 50 percent default rate. They kept them on portfolio, but they are lending to people who have substantial home equity. And so they come out okay, they collect a high interest rate as long as the loan performs.

And so we have to be very careful. What we saw in the crisis is—and to follow up on Deb's point there—what we saw in the crisis is, if you carve out—when you carve out exceptions—and we have strongly supported the provisions for the community banks in our filings with the CFPB and we work closely, particularly with the ICBA—but if you carve out blankets, the bad actors go to those places and try and use them.

And it has to be a balance. We won't create a perfect rule that stops all predatory lending. That can't be the goal because it will cut down too much credit. But we need to realize the bad guys know how to exploit those exception provisions, and they have done it and are doing it today.

Mr. DUFFY. But if the bad actors retain that risk; I think you have a whole different scenario.

Chairwoman CAPITO. The gentlemen's time has expired.

Mr. DUFFY. I yield back.

Chairwoman CAPITO. Ms. Waters for 5 minutes.

Ms. WATERS. Thank you very much, Madam Chairwoman.

Mr. Calhoun, the Consumer Financial Protection Bureau has been working very, very hard to make sure that they produce the regs, the rules to implement Dodd-Frank. On May 29th, the CFPB announced several amendments to the original ATR rule.

The first amendment clarified that compensation paid from a mortgage originator that is a bank or brokerage firm to one of its employees would not be counted toward the 3 percent points fees cap.

The second amendment exempted State housing finance agencies, nonprofits, and other community development groups from the QM rule if they make fewer than 200 loans per year and those loans are to moderate- or low-income consumers.

The third amendment makes it easier for community banks and credit unions with less than $2 billion in assets to make QM loans. If they make fewer than 500 first lien loans per year, and hold those loans in portfolio, they are not required to comply with the 43 percent debt-to-income ratio under the rule. These same lenders have also been granted a 2-year reprieve on the ban of balloon loans while the CFPB studies the issue further. And I guess that would refer to the rules.

Would you say that these amendments are an example of how hard the CFPB is working to make sure that we make good sense out of all of this? Do you think this is reasonable?

Mr. CALHOUN. Yes, we supported those. And I think what is important is those are a continuation of what they have done throughout this rulemaking process. Industry asked for a broad

QM and some folks opposed that. The CFPB gave a broad QM definition. Industry asked for bright line rules. And I think this is important when you talk about what is going on with access to credit. If you look at surveys, even of the members here, the number one thing holding back credit, home credit, is buy-back claims, not borrower claims on ability-to-repay. Buy-backs are when investors, whether they be the GSEs or private investors, force lenders to buy back the loans.

And this is the real key. Under the law, they are entitled to force those buy-backs if there is any variation in the loans. They don't have to show that is the reason the loan went into default. There have literally been tens of billions of dollars of buy-back claims paid, not just brought. And that is really what is pushing. I know the FHA has announced that they are going to start rulemaking to reduce the buy-backs and to clarify that. The GSEs have done some work, but really need do a lot more, because that is the real steam right now that is pushing in credit so much. The QM rule isn't even in effect yet and hasn't been over the last year and a half.

Ms. WATERS. Thank you. One moment, Mr. Calhoun. I want to get to Mr. Gardill.

Mr. Gardill, do you agree with these amendments that have been made by the Consumer Financial Protection Bureau?

Mr. GARDILL. I don't think the amendments cure the problem that we have.

Ms. WATERS. Would you like to go back to the way we were prior to the subprime meltdown and just leave you guys alone and not have a Qualified Mortgage rule at all? Is that what you want?

Mr. GARDILL. I am not asking for that.

Ms. WATERS. What were you asking for?

Mr. GARDILL. I think what we are asking for is that we be given the opportunity to provide flexible lending products to meet the needs of our customers as a community bank, and these rules don't give us that flexibility.

Ms. WATERS. You had that flexibility before the subprime meltdown and you almost brought this country to its knees—

Mr. GARDILL. No, I don't—

Ms. WATERS. —with a depression almost.

The question becomes, with the Consumer Financial Protection Bureau working very hard, coming up with amendments, trying to make sure that they address your concerns, the question really is specifically what more do you want?

Mr. GARDILL. I think we need to look at the forest. To equate it to a forest, if we have a couple of bad trees, we don't want to burn the forest down to correct that.

Ms. WATERS. I don't want to talk about the forest and the trees, I want specificity.

Mr. GARDILL. And that is what we are trying to do. We are trying to provide some input here today in good faith to assist in the process. And I think the fact that we are having this meeting and this hearing indicates that there is so much uncertainty that we are going to affect, adversely affect the housing recovery, that we need to step back and give ourselves more time to evaluate the impact of the rule and work with the CFPB to come up with better rules that retain the flexibility—

Ms. WATERS. Let me submit to you, Mr. Gardill, that the Bureau is working very, very hard. And it appears that there are too many who are willing to go around the regulators and come here and try and convince Members of Congress that somehow our attempt to address those concerns that this country all faced with the subprime meltdown, somehow you want to not deal with that, you simply want no rules, no rules to deal with the problem. And you still have not been specific about what it is—

Chairwoman CAPITO. The gentlewoman's time—

Ms. WATERS. —given these amendments, that you want to do. I yield back.

Chairwoman CAPITO. Mr. McHenry?

Mr. MCHENRY. I thank the chairwoman.

Mr. Calhoun, in your previous question they asked about, you said you wanted a permanent Federal exemption for the GSEs under QM. Is that right.

Mr. CALHOUN. We believe that we—

Mr. MCHENRY. Yes?

Mr. CALHOUN. We have supported lending above 43 percent—

Mr. MCHENRY. No, no, no, but you said you wanted a permanent extension for GSEs. So then, a separate question just to get this on the record, do you support the permanent existence of Fannie and Freddie?

Mr. CALHOUN. When we say for GSEs, I mean for them or their, the various bills that are out that have some sort of—

Mr. MCHENRY. Oh, okay, I just wanted to make sure we had that on the record just to understand, because some of us have concerns about keeping Fannie and Freddie around as they currently exist.

Mr. CALHOUN. Many of us do.

Mr. MCHENRY. Thank you for answering that.

But, Mr. Gardill, in your written testimony, to follow on to Chairwoman Capito's question, you mentioned that financial institutions are being encouraged to go into the non-QM space, right? And there are some concerns about liability. You reference that it would run counter, if you are held to the QM box as an institution, that would limit your ability to meet the Community Reinvestment Act obligations on institutions. Is that correct?

Mr. GARDILL. That is correct, Congressman.

Mr. MCHENRY. So out of that there is some fear that examiners would have some problems with that and some difficulty reconciling the two. Can you explain?

Mr. GARDILL. As I mentioned, some of our CRA-related programs will not qualify under the QM rule. We add liability under the ability-to-repay rule, now we have a serious issue whether we can do those loans.

I am also concerned about the regulatory impact of that, how are the regulators going to look at non-QM loans when you have liability? Do you have to establish reserves for those liabilities? So it creates a whole world of uncertainty.

What we retain those portfolio loans, which we do on our CRA loans that we have in our communities, and we have targeted programs for low- to moderate-income borrowers, but also low- to moderate-income neighborhoods where we are trying to maintain housing quality, and that goes to income borrowers of all sizes. We are going to have an issue whether we can make those loans at all. Then we will have an issue as to whether or not we can meet the Community Reinvestment Act requirements. If we can't do the CRA loans, how will we meet those requirements? So it is a Catch-22 from a regulatory perspective for banks in compliance.

And our purpose is to support our communities, that is what community banks do. Many banks provide community support. This straitjacket that we are being put in will limit our ability to design the programs necessary to meet the needs of our customers.

Mr. MCHENRY. So the Federal Reserve, in their ability-to-repay rule, didn't consider debt-to-income ratios as a very important predictor of the success of a consumer's ability-to-repay, right?

Mr. GARDILL. That is correct. And it very clearly is not set out—

Mr. MCHENRY. So what is the strongest metric for success in ensuring that a borrower can repay their mortgage?

Mr. GARDILL. It takes not only the ability-to-repay, but adequate collateral to support the loan; it is a two-sided equation. So there has to be value and there has to be the ability-to-repay, but we can't create a straitjacket in how to measure that ability-to-repay by arbitrary rules that narrow what you can consider. Banks do a balanced approach in measuring credit, and that is what we want to retain. The rules don't do that for us.

Mr. MCHENRY. So, Mr. Reed, to that point, you mentioned in your testimony that you have credit unions that will lend with debt-to-income ratios of 45, 50, percent and their loan losses or mortgage losses remain very low. Why is that?

Mr. REED. Credit unions are very unique, as I mentioned earlier, in our structure and our purpose. But I would like to address that in a broader perspective.

Mr. MCHENRY. I have 20 seconds for you.

Mr. REED. Yes, okay. So let me just say, I have underwritten loans, mortgage loans for 25 years. Let me tell you something fundamentally. The difference here is, we are focusing when we say, hey, we don't like this, because you are focusing on product features—no-doc loans, loans that weren't violating previous regulations that were already set by agencies which were underwriting guidelines.

As already mentioned today, the FHA has a lot of leniency to address a lot of disparate impact issues and has been doing that very successfully for years. The people who were defaulting were the people being put into products that should have never been put into those products. That is the fundamental fee here.

I think the CFPB has done an excellent job in eliminating those products that are not correct. But I don't think the CFPB is doing any of us or the country any good by restricting the underwriting criteria that put people who are creditworthy, for example, who want two or three jobs and can do it.

Chairwoman CAPITO. I am going to have to stop you here. The gentleman's time has expired.

Mrs. Maloney?

Mrs. MALONEY. I agree wholeheartedly with the point that many of you are making that we shouldn't have one-size-fits-all and every borrower should not fit into one box. But I can recall during the hearings the commonsense belief by many of us is that you shouldn't put someone into a loan they can't afford. It is going to hurt the banks, it is going to hurt the economy, and it is certainly going to hurt the homeowner. And I feel that is what the CFPB tried to do, is to really come up with some standard where people don't buy something they can't afford. And it would include all of the income that you mentioned. You can be working three or four jobs; many of my constituents work two jobs.

But I do think that they tried to be flexible; they came up with three exceptions. The exception for compensation for mortgage originator is not included in the 3 percent points and fee cap, it exempted nonprofits from the QM rule if they have fewer than 200 loans, and lenders with less than $2 billion in assets may make the QM loans that do not meet the 43 percent debt-to-income ratio.

And so, those are several of the exceptions that they have made. They may have made more. What other specific exception do you think should be made, Mr. Thomas and Ms. Still?

Mr. THOMAS. I am going to yield to Ms. Still because she is better prepared.

Mrs. MALONEY. Okay. Ms. Still?

Ms. STILL. Thank you. Yes, so in terms of underwriting, I think the CFPB has done a fine job providing for the temporary QM. I think, though, when you look at the 3 point rule and you look at some of the inclusions still in the 3 point rule that have nothing to do with the consumer's ability-to-repay, that is where it becomes prohibited, particularly to the smaller loan amounts. So affiliate fees should not be included in the 3 point rule, nor should compensation paid to brokers.

Again, for any consumer who is getting the same rate, points and fees, the business channel should not matter. And so, the exemption should be on behalf of the consumer and a level playing field for all lenders serving finance in the United States.

Mrs. MALONEY. In the terms of that, just taking for one example the title insurance that you mentioned, and I believe Mr. Thomas mentioned, and Mr. Calhoun, and if I recall, you said it was regulated by the States and very competitive, and I believe you testified that the title insurance would be more expensive under the CFPB rule. And I would like to ask Mr. Thomas and Ms. Still why it would be more expensive, because I don't quite understand why?

And also, Mr. Calhoun, you talked about the affiliated title insurance and taking the position that it should be included in the points and fees, if I recall. So if all three of you could answer that on the title insurance, which is one example you all mentioned. Thank you.

Ms. STILL. As you did mention, title insurance is either regulated or promulgated by the State, therefore it is a very competitive environment in any given State. By eliminating or combining the affiliate fees, you eliminate the potential for competition, which is why the remainder of the market might get actually more expensive. There have been studies in the past, I believe there was one in Kansas about 6, 7 years ago that Kansas had tried to implement an affiliate fee, and the remaining competition actually raised prices.

Mrs. MALONEY. Okay. Mr. Calhoun, could you respond?

Mr. CALHOUN. This committee, just a few years ago, raised the issue of the problems in the title insurance industry and asked for a report that was put out in 2007 by the GAO finding it is a deeply troubled industry. As I indicated, whenever you have a situation where two parties are cutting the deal and the third party is paying the price, that third party, in this case the consumer, often comes out on the short end of things. And as I said, it works out well for the parties at the table. There is a big commission. Seventy-five cents out of every dollar is what the GAO found out goes to pay this commission, while only 10 cents goes to claims. In most insurance, that is 80 to 90 percent. So this is just taking a broken system that needs reform and making it worse.

Mr. THOMAS. If I could, the problem is this is a State-regulated institution, that being the title insurance, and it is very well-regulated, I can tell you, in California. At one time, there was a lot of money that was paid back to people as kickbacks and so on. Today, I can't even get a pen from a title company. It is so well-regulated that they have clamped down on everything. And if you open it up—or if you clamp down even more and say, okay, only the large title companies can do anything and you cannot have affiliated title companies, you are only going to open it up so that they can do whatever they want to do.

Ms. STILL. And I would argue that—

Chairwoman CAPITO. Excuse me, the gentlelady's time has expired.

We will go to Mr. Luetkemeyer.

Mr. LUETKEMEYER. Thank you, Madam Chairwoman.

One of the things that is kind of concerning to me is the very nature of a QM, because it seems like it is perverting the very thing you are trying to do, from a standpoint that we are trying to provide a save harbor here for lenders who if they go with a certain criteria are limited from the amount of liability they could incur if they are doing things right.

You would infer then that if those loans don't qualify for QM, suddenly now they would have more liability exposure, and if you have 50 percent of your loans that don't qualify for QM, now you have 50 percent of the loans on your books with problems.

Mr. Vice, you are a supervisor, how do you look at that?

Mr. VICE. That is a concern to us. We don't know exactly how that is going to be treated on examinations going forward. And that is one thing that the industry is kind of watching with bated breath to see. Once my first examination happens, if I have a non-QM on the books, how will regulators treat that?

Again, as I stated before, it is my hope that we don't treat that adversely, that we look at that and look at it on an individual credit basis. And again, our whole hope and our whole desire here is to make sure that we have a diverse marketplace where several lenders have the opportunity to meet the legitimate credit needs of the individuals who are there and we have to have that flexibility. And that is why we are seeking and applaud this small creditor qualification to QM.

Mr. LUETKEMEYER. I think that we are looking also for an exemption for community banks and folks like that who work with small numbers of loans.

Mr. Gardill, it would seem to me that if something doesn't qualify, it would really restrict the low- and moderate-income folks from the standpoint that they are the ones who are going to have probably the lowest credit ratings and have the most difficulty trying to prove that they can get into the QM box. It would logically seem to me that we are really restricting low- and moderate-income folks by doing this. What is your opinion on this?

Mr. GARDILL. Yes, I agree 100 percent. By extending liability to those under the ability-to-repay rule, it is going to greatly restrict our opportunity to do them at all. If the safe harbor applied to the ability-to-repay rule, it would be an improvement in the structure, because then you could safely make those loans. But the QM rule has a very narrow save harbor; it is not available under the ability-to-repay. And we are permitting borrowers to assert, back to your point about the QM, even challenge the QM qualification as to whether or not proper verification of debt to income was created. So, we create potential liability claim even under the QM rule.

Mr. LUETKEMEYER. It would seem to me that we are actually causing more risk here from the standpoint that the loans that are most risky, that have the poorer scores or have less ability to make—their income are less flexible, they are more on the edge, those are the ones that can't qualify for QM, yet those are the ones that, if you make the loan, you are going to have to hold them in your portfolio. It would seem to me to be a real problem.

Mr. GARDILL. And that is our principal concern, is serving our customers, and I am not sure these rules permit us to do that. That is really the issue, and that is why I think it deserves some time and study for us to evaluate this more carefully before we affect those most vulnerable in the communities that we serve.

Mr. LUETKEMEYER. I have about a minute and a half left. I live in a very rural area. I know that the chairwoman made a comment a while ago about the rural designation here. One of you made the comment a while ago, I think it was Mr. Vice, with regards to petitioning, have a petition process available so that we could get this rural designation fixed. I think each one of you in your testimony, most of you anyway, as I have gone through the testimony, seem to have pointed out inequities in the rural designation. Can you describe your petition process suggestion a little bit further, Mr. Vice?

Mr. VICE. I think one of the concerns from my perspective that occurred so far with this rural designation is that it is applying a formula developed in Washington. As the commissioner for the Department of Financial—

Mr. LUETKEMEYER. That never works anywhere on anything, does it?

Mr. VICE. —at the Department of Financial Institutions in Kentucky, I have not been asked what is a rural county in Kentucky. Same thing with the commissioner in West Virginia; they haven't been asked, either. So our petition process—and again this is the short-term fix, we think this actually requires a statutory fix to address this problem—but a short-term fix would be to let the CFPB establish a process where local authorities could give input on what is a rural designation. Let the local authorities give various stakeholders the ability to have input in that process before we take it to the CFPB. And then also, as a third follow-up piece to that, have a review process to make sure we got it right at some future point in time.

Mr. LUETKEMEYER. Very good. I thank you for your testimony today.

And I yield back. Thank you, Madam Chairwoman.

Chairwoman CAPITO. Thank you.

Mr. Hinojosa?

Mr. HINOJOSA. Thank you, Chairwoman Capito and Ranking Member Meeks. And thank you to our witnesses today for sharing your valued testimony.

As the Consumer Financial Protection Bureau has continued in the process of crafting the Qualified Mortgage rule, industry advocates have raised valid concerns and the Bureau has listened. For example, industry questioned why certain payments were double counted towards the points and fees cap, and the Bureau altered the rule accordingly. Additionally, manufactured home industry advocates found issue with the 3 percent cap and it was modified as well.

My first question is for Mr. Calhoun and Ms. Still. I would like to ask you about the lack of mortgage credit for rural areas. As chairman of the Rural Housing Caucus, I am very concerned that housing in rural America is becoming progressively more neglected. The USDA rural housing programs are critical to ensuring a quality housing stock in areas with high need, such as my district in deep south Texas. The Bureau recently wrote a rule granting exemptions for rural areas from the balloon payment prohibition. However, the definition excludes all of Hidalgo County, with a population of 850,000 people, which is in my district and is home to more than 700 Colonias, which is higher than any county in United States. Colonias, for those who don't know the word, are communities which lack basic infrastructure and often suffer from deplorable housing conditions.

So, Mr. Calhoun and Ms. Still, do you feel that this rural definition is adequate, and does the Bureau need to do more to accommodate rural area lenders?

Ms. STILL. Yes. We would agree with you that the Bureau has been a good listener of the industry and has responded to feedback. I believe the Bureau just in the last couple of weeks has suggested that it needs to continue to study the definition of rural, very appropriately so, and the MBA looks forward to working with the Bureau on helping with that definition.

In the meantime we certainly need clarity around that, and I would suggest that when you look at the challenges for rural, it centers largely on smaller loan amounts, it centers largely on the community lending that possibly small community lenders and brokers do. And so, we need to look at all of the issues that are making up the problems for rural housing and address that in the entire rule for every consumer.

Mr. HINOJOSA. Mr. Calhoun, would you answer that, also?

Mr. CALHOUN. Yes. We agree that the CFPB has been a good listener, it has responded and even used its exception authority for a number of those rules that you mentioned to expand it. We have supported a very broad rural definition and are glad to see that they are going to look at that further, and we are pretty optimistic and the indications are they know they need to do better on that.

If I can quickly add, I think one point that has been lost here—people are acting as if we are going into this strange land and have no experience about what life would be like under these rules. We have a lot of experience. These rules are very similar to rules that have been in effect with similar fee limits at States for decades, and loans, including small loans, were made. As we sit here today—

Mr. HINOJOSA. Let me remind all of you that the farm bill has been debated here in the House, it is before us now in the House of Representatives, and they are not answering the question about the definition of the rule so as to help rural America appropriately. And you all need to step it up and help us get that definition to where it does address it.

Mr. CALHOUN. We agree.

Mr. HINOJOSA. My next question is for Gary Thomas and for Debra Still. My question is, in your testimony you note that title insurance is a competitive market, and that by putting affiliated title companies at a disadvantage, prices might increase for consumers. However, you also state that title insurance pricing is well-regulated by the individual States. If that is the case, why do you think title insurance would be more expensive under the current CFPB rule?

Mr. THOMAS. Once you eliminate competition, you come down to just a handful of players in any specific area. They can start going to the States and asking for higher rates and probably proving those up in the way they want to. And so, you have really restricted the number of players in the entire spectrum, you are going to have higher rights.

Mr. HINOJOSA. Ms. Still?

Ms. STILL. I would agree with that answer fully, this is the ability-to-pay rule, this is about a consumer's ability to repay. So when we talk about the title insurance business, this should not have anything to do with that industry. This should have to do with a level playing field for affiliates and the fact that consumers have lost their ability to shop if the affiliates are treated in a disparate fashion.

Mr. HINOJOSA. That answer justifies why REALTORS® are so concerned, and I think we need to address that question.

Thank you, Madam Chairwoman.

Chairwoman CAPITO. Thank you.

Mr. Pittenger for 5 minutes.

Mr. PITTENGER. Thank you, Madam Chairwoman.

In light of the concerns that have been expressed today regarding the ability-to-repay, the QM rule, as relates to the mortgage credit crisis that could evolve, what changes do you think should be made to the Dodd-Frank Act on the ability-to-repay QM provisions that this committee should be considering? I will start with Mr. Gardill, but any if others want to respond, I would welcome that.

Mr. GARDILL. I think principally, we are looking for some flexibility of the verification rules. We want to work with the CFPB to get this right so that we don't adversely impact our customers or the recovery in the housing market that we are experiencing. I think we have to revisit the liability rule. The liability rule under the ability-to-repay is onerous. Permitting oral testimony after the fact, an unlimited statute of limitations, those things will restrict lending, they will restrict our ability to do that, they will affect our regulatory compliance. So that is for a start, I think.

Ms. STILL. I might suggest that the spirit of the bill is fundamentally sound. The fact that we should verify that the borrower has the ability-to-repay, fully doc loans, taking away some of the extraordinary loan programs of the past. But H.R. 1077 fixes such an enormous amount of the problems with the ability-to-pay rule, and that would go such a long way.

I also think we need to look at the hard stop 43 back ratio on jumbo loans, we need to look at the APOR index and the problems with that. And I think we need to look to Mr. Gardill's comments earlier on industry readiness, and if the industry isn't ready, will consumer lending stop or real estate finance stop in the short run and derail our housing recovery?

Mr. REED. I just would like to add, too, that I think, based on all of my colleagues' statements today, that we should make permanent and not be temporary the saleability of those loans to the GSEs. This is a huge issue and it is creating a tremendous amount of instability in the market presently because of this temporary period.

Those regulations and those guidelines that were already established for years in the other agencies have served us well and it hasn't been the underwriting criteria per se as much as the product features where we were not documenting loans and we were not asking for assets, we were not verifying income.

The CFPB has addressed those issues. And I agree with Ms. Still that the spirit of the bill is where it needs to be, but we need to tweak it in those areas and set up those guidelines or those metric points so that we can retain our flexibilities. And that is, I think, what we are really asking here, is we need to be able to retain the flexibilities we have enjoyed previously.

Mr. PITTENGER. Anyone else?

Mr. THOMAS. Yes, I would like to comment, too. What we are facing if we don't get this right is pretty much what we are facing right now, and that is the instability in the marketplace. As a street REALTOR®, what we are facing right now is 30 to 40 percent of the purchases are all cash. Where is that all cash coming from? It is coming from investors and it is coming from offshore. If we don't get this right, you are shutting out the first-time home buyer and the underserved homeowners who want to get back into home ownership.

And so, we are really talking about a severe sea change if we don't get this right. We are going to have more and more investors investing in the marketplace, turning what used to be homeowner properties into rentals, and you are going have a big change in the whole socioeconomic makeup of this country. So we have to get it right.

Mr. PITTENGER. Mr. Calhoun?

Mr. CALHOUN. If I may add, I would agree with Ms. Still that the basic statutory framework provides the necessary mechanisms and tools. We have a regulator who is data-based and who is listening.

I think these oversight hearings are not just appropriate, but necessary as part of that process to raise concerns and to have the agency answer as to how they are addressing them.

I would point out that those houses that are being bought today are houses that were foreclosed upon because there weren't protections in place, and that is how we ended up in this mess.

Mr. PITTENGER. I have 15 seconds. Mr. Vice, do you want to say something?

Mr. VICE. The main thing I was going to say is if you are looking for a bright line of how do we change Dodd-Frank, I would make sure that it aligns with the business models. It is a completely different business model to originate a portfolio and sell it, and it is a completely lending aspect if you originate a loan and you are going to keep it in your portfolio because then the interest aligned between the borrower and the creditor. And there is a much different lending atmosphere. In Mr. Reed's written testimony, you will see that there is a lot less credit risk associated with loans that are held in portfolio.

Mr. PITTENGER. Thank you. I yield back my time.

Chairwoman CAPITO. Thank you.

Mr. Scott?

Mr. SCOTT. Thank you very much, Mr. Chairman.

Mr. Calhoun earlier made a statement that I totally disagree with, and that is on his issue of the need for H.R. 1077.

Let me assure you, Mr. Calhoun, we desperately need H.R. 1077. Some of the very people you were talking about, some of the lower-income African Americans, and not just them, but everybody—dealing with a home purchase in real estate is the most complex, most difficult transaction that 90 percent of the American people will ever go through. And you know what they need the most? Information. Information makes them powerful; it helps with the problems. That is why we have so much predatory lending.

House Resolution 1077 does some essential things. First of all, it strengthens the Truth in Lending Act. It will require for the first time that customers and potential homeowners will receive information dealing with points, not maybe, not if, but they must be told information about points, about fees, about all of the loan modifications available to them.

I represent Georgia and the suburbs of Georgia, at one time the leading part of this country with home foreclosures, and the number one problem they had was, "I didn't know." Well now, under H.R. 1077, they will know. This is vital information. This is an important bill.

Mr. Thomas, I would like for to you address that, and Ms. Still, as to why House Resolution 1077 is very important.

Mr. THOMAS. What it does is it levels the playing field. It makes it more open to more players in the marketplace. If my constituents, meaning other brokers, want to have a title company affiliation, if they want to have a mortgage affiliation, let me tell you, first of all, that the REALTORS® in that firm don't necessarily flock to that title company or lender that the broker owns, because they are going to hold them to a higher standard. They want to make sure that their customer is best-served. And whether it is the in-house lender or it is somebody else, they want to make sure that their consumer is handled properly because they want to have future business that is a referral from them.

And so, we want to make sure that we have as many players in the marketplace in a level playing field rather than just bringing it down to a few, which is what we would have if we don't pass H.R. 1077.

Ms. STILL. Competition is good for consumers and we need as much competition as possible. We also need consumers to be able to have a choice of their settlement service provider. And we also need transparency in shopping, to your point. It has to be a level playing field or the consumer is not going to know how to shop. The bill is critical to level the playing field, and thank you for cosponsoring it.

Mr. SCOTT. Thank you very much.

Chairwoman CAPITO. Thank you.

Mr. Barr for 5 minutes.

Mr. BARR. Thank you, Madam Chairwoman.

Mr. Gardill, this is a question for you. You included in your written testimony the following statement, "The QM box ironically may conflict with fair lending rules and goals of the Community Reinvestment Act. And it is quite the Catch-22 when a bank attempts to limit its regulatory litigation and reputational risk by staying within government prescribed rules only to be subject to possible regulatory litigation and reputational risks for not straying outside those rules."

Do you think it is possible for financial institutions to meet their CRA obligations while issuing only QM loans?

Mr. GARDILL. No, I think it would be extremely difficult to do so.

Mr. BARR. Would you view the QM rule as it is currently structured to be basically, in effect, a partial repeal of CRA?

Mr. GARDILL. It is going to impact the bank's ability to comply. The CRA is still there, we still have to meet that regulatory burden. Just for example, last year we did 203 loans, CRA eligible, about $17 million, and not one of them would meet the QM rule.

Mr. BARR. Ms. Still, a follow-up question for you on the same topic: What do you believe is the implication of QM on the disparate impact analysis?

Ms. STILL. The industry desperately needs clarification on how to comply with two rules that seemingly might bump up against each other. And so of course, the industry deplores discrimination in any fashion; it is very committed to complying with the disparate impact rule. But if the lender chooses only to lend on QM loans, it could be in violation of HUD's disparate impact rule. So we need the regulators to work together and help the industry understand how to negotiate that situation with which we are faced.

Mr. BARR. I appreciate the testimony of both of you in highlighting what appears to be a dramatic contradictory mandate coming from the regulators, that you have a CRA obligation on the one hand, but, Mr. Gardill, as you pointed out, it is a Catch-22 for the lender in this situation when you all are obligated to originate QMs to obtain the safe harbor and then also expected to somehow satisfy this disparate impact analysis.

I want to move now to Commissioner Vice and your testimony. And if staff could put up on the screen a picture of the Commonwealth of Kentucky?

[slide]

Mr. BARR. And this is kind of a follow-up to Mr. Luetkemeyer's question about the CFPB's rural designation. If you take a look at this screen, you can see a county-by-county map of Kentucky. And the counties in yellow, Commissioner Vice, are the counties that the CFPB recognizes as nonrural and the counties in blue are counties which the CFPB has classified as rural.

This is obviously relevant to our hearing today because the CFPB has established a category of QMs with balloon payments that are originated by small creditors in rural or underserved areas.

You will notice—and you are from Clark County, sir, so you are familiar with this geography—Bath County, which is just two counties over from you to the east. Can you share with the committee and with your colleagues on the panel, Bath County, and is it a proper designation to categorize Bath County as nonrural?

Mr. VICE. I have actually had the distinct pleasure of being the examiner in charge of a couple of banks that are headquartered in Bath County. Everything about Bath County is rural and it should be considered rural. Even if you look at the population disbursement amongst the area, it should be considered a rural county.

The community itself, there is a lot of ag-based businesses there. There is not a whole lot of industry in Bath County as well. So Bath County, out of any county in Kentucky, should be considered rural.

Mr. BARR. So I think, Commissioner, this is exhibit A for your position that there needs to be some kind of petition process to fix the rural designation.

A quick follow-up for you, Commissioner. Does the CFPB, in your judgment, have the statutory authority to do this or does Congress need to intervene here and give the CFPB the authority to implement this petition process you propose?

Mr. VICE. It is our opinion that the CFPB currently does have the ability to do the petition process.

Mr. BARR. If they continue to rely on the various government definitions of rural, would you recommend to this committee and to this Congress to statutorily implement a petition process?

Mr. VICE. We would either like to see a statutory implementation of it or the Dodd-Frank Act be amended to move the reference to rural in the balloon loan category.

Mr. BARR. Okay. And then I guess one final question, as my time is expiring. As a bank supervisor, Commissioner, could you just briefly amplify your testimony that Congress should create a general statutory small creditor QM and apply it to all loans held in portfolio?

Mr. VICE. Yes. We think this is very important in that small community banks'—and again, their interests align when they are originating a loan—primary focus is to create, for lack of a better term, to borrow something from Steve Covey, a "win-win situation." What are the borrower's credit needs and how can we meet those to create a loan to meet those needs.

Mr. BARR. Thank you

Chairwoman CAPITO. Mr. Capuano?

Mr. CAPUANO. Thank you, Madam Chairwoman.

I want to thank the panel members for being here today.

I just have a question for everybody. And, again, we are talking a lot of details here, and that is fine, but to me the generalities of how we get here is also important.

Does anyone on the panel disagree with the statement that prior to 2008, there were a fair number of mortgages given in this country that should not have been given out? Does anyone disagree with that statement?

I didn't think so. So, everybody agrees that prior to 2008 there were a fair amount of mortgages that should not have been given. Fine.

Mr. Gardill, on page 11, you make a statement that I agree with, but I wonder what it means. It says, "These rules will restrict, rather than facilitate, credit to mortgage borrowers, particularly borrowers on the margins."

Isn't that the whole point, that borrowers on the margins are the ones who got those loans in 2006 and 2007 and 2008 that we should not have been giving, and therefore the borrowers on the margins are the ones who should not get mortgages in the future? Should we not be restricting some of those, or should all borrowers on the margins be given mortgages at all times?

Mr. GARDILL. I think we have to be careful how we generalize and preclude from our homeowner system in this country, otherwise qualified borrowers—

Mr. CAPUANO. I understand—

Mr. GARDILL. —with the flexibility that they could own a home and we can successfully provide credit.

Mr. CAPUANO. I fully understand that. As a matter of fact, the other side criticized people like me for pushing that for years, actually for generations, that I thought more people should be qualified, but now, in light of 2008, I realize there is a line somewhere. I am not sure exactly where that line is. But do you agree that there is a line that at some point a borrower should not get a mortgage?

Mr. GARDILL. And that is the reason I think we need some time; we are looking for an extra year here in order to make sure that we get it right.

Mr. CAPUANO. I don't disagree. I want to get it right, too. I actually think that the comments that were made earlier on competition and choice and level playing field and coordination of regulators are all 100 percent correct. I am not looking for one mortgage originator, I am not looking for no choice, I am not looking for that one person to do it all. That would be wrong, and it wouldn't help anybody. So, I totally agree with those comments.

I guess what I am trying get at is that we all seem to agree that there should be some restrictions. The question is, where should those lines be and exactly how does it all work? And we are all working on presumptions as to what they should be.

I guess the question that I really have is, when everything is said and done, based on what you know—and I assume every one of you was active in this area before 2008—if there was 100 percent of the people, 100 percent of the people who got mortgages in 2008, what percentage do you think should not get mortgages?

Where should that line be? Should it be 100 percent? Should it be 110 percent? Should it be 70 percent? And I ask you because there is a study out there that suggests that the CFPB's proposal will cut out something like 48 percent of the mortgages, which I think anybody would agree that, if that is correct, it is too high.

I guess I am asking, what would your goal be? And we may as well just start with you, Mr. Vice. What would your goal be, starting in 2008, if that is equal to 100, what would it be? Should it be 95 percent? Should it be 75? And, again, general, and I am not going to hold it to you. I am just trying to get a general idea.

Mr. VICE. I would be hesitant to look at it that way, and the reason I would be is in 2008, let's take your example, 100 percent of the population who got more mortgages, some of those people may have been able to afford a mortgage, just a lower amount, but they were given the ability through a product offering to get a mortgage that they couldn't afford, because it was too high.

So I don't think we should be looking at this or asking the question, you don't deserve a mortgage, you shouldn't get one, and this percentage should not have gotten one. I think the question should be more of, how do we make sure we are aligning the interests between the borrower and the creditor to make sure that the correct credit decision is made for that borrower?

Mr. CAPUANO. The only thing I am interested in is having no more taxpayer bailouts for people who give out mortgages.

Mr. VICE. I agree.

Mr. CAPUANO. That is my main category. And achieving the highest percentage of homeowners as possible with that as the knowledge. But you are telling me that everyone who got a mortgage in 2008, somehow, somewhere, could have been and should be qualified to get a mortgage today?

Mr. VICE. No. I think—

Mr. CAPUANO. So that there should be some percentage who shouldn't. And I understand you may not have a number.

Mr. Gardill, how about you? Do you have a general idea, a range?

Mr. GARDILL. I think we have to look at the issues. I don't think you can arbitrarily set a bright standard or a bright line.

Mr. CAPUANO. I am not asking for a bright line.

Mr. GARDILL. We had a rapid acceleration in value and a rapid deceleration in value, and what we are trying to do is avoid that—

Mr. CAPUANO. So I guess I am not going to get an answer. Does anybody want to jump in with a number? I didn't think you would, but I figured I would ask anyway.

And the reason I ask is because that is what we are here for; no one wants 48 percent of the mortgages to not get access to credit. That is not good for anybody. But there are some people who should not get a mortgage. And I guess for me the question is, what is that goal? Because what I am hearing in the general testimony is that these proposals will shut off credit to too many people. Fine. That scares me, as it should. How many will it shut off credit to? Go ahead.

Ms. STILL. But I think we need to be careful with context, because when you talk about the margins in 2006, 2007, and 2008, it was a very different margin than in today's overly tight credit conditions. So when we talk about deserving borrowers in 2013 who may not get mortgages, it truly is a deserving borrower.

I believe that the law, by prohibiting exotic loan programs, by mandating that lenders fully document income and assets, no more stated income loans, go an enormous way to helping the consumer make a good, well-informed decision with good counseling from a lender. So I just think we need to be very careful that it is not the same margin. Thank you.

Mr. CAPUANO. I totally agree that we need to be careful, and that is what we are doing here.

Madam Chairwoman, I know I am over my time. I apologize, and I appreciate your indulgence.

Chairwoman CAPITO. Thank you.

Mr. Miller?

Mr. MILLER. Thank you, Madam Chairwoman.

I respect my good friend's concerns on making loans that are not predatory. In fact, in 2001 I started introducing amendments to bills and said, let's define subprime versus predatory. I think it got to the Senate 5 times, as you recall, and they never took it up, or we might not have had some of the problems we had.

I guess the definition of margins would be when you apply them to. And I think if you go back to 2006, 2007, and 2008, the margins were not margins, they were just, could you sign your name, you are qualified. There were no underwriting standards.

But my biggest concern is the CoreLogic study in 2010, because those loans were not being made in 2010. In fact, the CoreLogic study shows that the loans made in 2010 were very good loans. My good friend, the ranking member, Maxine Waters, brought up a concern she had that people were going to be limited from the marketplace. And I think, Mr. Calhoun, you said that based on the flexibility that is allowed through QM, the GSE would still provide the loan. So 95 percent of the loans that they said wouldn't be made would be made.

The problem I have with that, and I am not impugning you, is that Secretary DeMarco came right before this committee, as all of you recall, and said that GSEs will not be allowed to go outside of a strict QM definition. So your response to defining the study that was given to us by CoreLogic would not be applicable based on his definitive comment to us, and that is where my concern comes from.

If they are going to go strictly by the guidelines of QM and not be allowed flexibility, which he said without a doubt they are going to be required to do, half of those loans made in 2010 that are performing very well would not be allowed to be made today. That is what the debate is on today, not whether we made bad loans in 2006, 2007, and 2008, because we did. The underwriting standards then were just, especially through Countrywide, can you sign your name, you met the underwriting standards. That is how bad they were.

But, Ms. Still and Mr. Gardill, what impact would this have on housing today, this strict requirement, especially by DeMarco and the GSEs, that they are going to have stay within QM? How much impact is it going to have on the market today?

Ms. STILL. I don't know an exact number for you.

Mr. MILLER. Does it drive more buyers to FHA, which we are trying to eliminate buyers from FHA, I guess is the other guideline.

Ms. STILL. Yes. Any borrower, because the points and fees test is a test that will determine QM or non-QM, any borrower who cannot meet the points and fees test will no longer now be eligible to be sold to a GSE.

Mr. MILLER. And they are going to go over to FHA, which is increasing the burden on FHA, which we are trying to decrease the burden on FHA? We are creating a—

Ms. STILL. The FHA program will be mandated to meet the points and fees test as well. So the points and fees tests have to be met regardless of the investor. It will be private capital that would choose to do that non-QM loan, and we don't think there will be a lot of private capital at all. And if there is, it will be only for the highest quality borrowers, not for the broad middle-class America.

Mr. MILLER. Whether you support GSEs or not, if they are out of the marketplace in this market, it could be devastating.

And the ability-to-repay rule purpose, it is very clear to me, and it sets guidelines to approve a borrower's ability-to-repay, but I don't know where the 3 percent cap on points and fees falls in that at all. The 3 percent cap in fee has nothing to do with the borrower's ability-to-repay. And I look at what is included in the caps, how does escrow insurance relate to the person's ability-to-repay? Some title insurance is included, but other title insurance is excluded depending on who pays for the policy. Mortgage origination fees are included when a mortgage broker is used, but not when a loan is originated at the bank or credit union. Nonprofit creditors are exempt from all the caps completely.

So if there are so many exclusions and the exclusions are based on who you are, what does this do to the underlying issue of trying to create a safe and sound loan? I guess, Ms. Still, I would go back to you again to let you answer that if you can.

Ms. STILL. We would agree that the points and fees cap and some of the fees that are included in have nothing to do with the ability-to-repay. It has to do with a business channel. And we believe all of that should be a level playing field, which is why it is so important to pass H.R. 1077.

Mr. MILLER. It is beyond that. You are discriminating against certain groups. For an example, if you are a non-profit creditor, you are exempt completely. If you are a mortgage originator, you are included when a mortgage broker is used. So if you are a mortgage broker, you are going to be inclined not to use a mortgage broker, because I am penalized if I do. But when a loan is originated by a bank or credit union, well, I don't have to comply.

So I am really bothered by anything we do that discriminates against anybody or any group or organization or it picks winners and losers. So you can say, really I can save myself some money and not be—not save money, but I could be exempt from all this if I just use a nonprofit; or if I don't use a mortgage broker, the loan can be through a bank or credit union, then I have no fees or caps.

If you just look at that alone, you have to say something is seriously wrong with the structure when we pick winners and losers and we discriminate against some and not others. So I think that is something that we seriously need to look at.

And I yield back the balance of my time.

Chairwoman CAPITO. The gentleman yields back.

I would like to ask for unanimous consent to insert into the record written statements from the Consumer Mortgage Coalition, the National Association of Federal Credit Unions, the Independent Community Bankers of America, the Community Associations Institute, and the American Land Title Association. Without objection, it is so ordered.

Mr. Ellison?

Mr. ELLISON. Thank you, Madam Chairwoman. And thanks to the ranking member and all of the witnesses today. It is an important issue, and you all have helped us understand it better.

Ms. Still, I wanted to ask you a question. I believe you recommended allowing higher fees for loans up to $200,000. What percentage of home sales and refinances for mortgages below $200,000? If we were to follow your idea, who will we be affecting?

Ms. STILL. I believe the right way to fix the points and fees problem is H.R. 1077, but another alternative way would be to raise the tolerance of the definition of a small loan from $100,000 to $200,000.

And as I look at all of the loans that I made last year, which was to about 12,000 customers, I would tell you that the points and fees start tripping at about the $160,000 to $180,000. If we were to go to $200,000, we would probably solve about 90 percent of the problem, based on the data that I have looked at in my company. So it is another way to raise the definition of a small loan and more borrowers would be included in the QM definition.

Mr. ELLISON. Do you want to respond to that, Mr. Calhoun?

Mr. CALHOUN. Yes. First of all, I think it is important that people have asked, what do fees have to do with this? The Financial Crisis Commission found that high fee loans contributed to the crisis, because lenders are collecting their revenue at closing, not through the performance of the loan. It misaligns the borrower and the lender incentives there. The lender wins by charging the high fees at closing. This bill would far more than double the fees that could be charged and still be a QM loan.

Mr. ELLISON. Excuse me. When you say, "this bill," you are referring to H.R. 1077?

Mr. CALHOUN. H.R. 1077.

The other point is people are acting as if an ability-to-repay rule is something new. All loans that have over 150 basis points of interest rate over APOR, which is significant ones, are currently subject and have been for the last several years to an ability-to-repay rule under the Federal Reserve rules with no safe harbor for any of the loans, and the sky didn't fall. I asked people, tell me of these lawsuits. No one can point to a single one, much less a flood of them.

So Congress based this ability-to-repay rule off of what the Federal Reserve had done before Dodd-Frank was passed. We have experience under that. It worked. This rule has a lot more industry protections than the Federal Reserve rule did. It has a safe harbor for most of the loans. The Federal Reserve rule did not have a safe harbor for any of the loans.

Mr. ELLISON. Okay. Anybody else want to weigh in on that question I asked? You don't have to.

Ms. STILL. The only thing I was going to mention is my MBA colleagues behind me tell me that the average loan amount in America is $220,000, which is why the $200,000 is a relevant number.

Mr. ELLISON. All right. Thank you.

Mr. Calhoun, I have a question for you. How would a consumer comparison shop for title insurance? How many title insurance firms are there nationwide? If you wanted to go for the lower price, could you do it, given current standards?

Mr. CALHOUN. As the GAO study found, there is virtually no shopping for title insurance. And I find that is true even when I ask financial and mortgage professionals did they shop for title insurance. They don't market to consumers; they market to other industry professionals, because those are the ones who select the service. And, in fact, there is little or no price competition. Everybody tries to charge the maximum rate.

And lenders who are larger—Ms. Still's operation can have 125 people who focus just on title insurance. That gives them an edge over those who can't do that. We already have five lenders who control more than half of all mortgages in this country. Now you want to hand the title insurance to them also and encourage that? That doesn't seem like it makes a more competitive market.

Mr. ELLISON. Do home buyers know that they are paying a commission?

Mr. CALHOUN. My experience has been virtually none do, much less that the commission is 75 percent of the premium. For a $500,000 loan here in the District, the insurance premium for just the bare-bones coverage is about $3,000. The commission part of that in the District is about $2,200 going to the person who picks the policy even though they charge you separately for the other title work.

Those are the kinds of facts that led the GAO to raise grave concerns about the title insurance market. And as I said, instead of fixing it, this makes it worse.

Chairwoman CAPITO. The gentleman's time has expired.

I thank all of the witnesses, and I would like to thank the ranking member, as well, for his attention to this very important issue.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

This hearing is now adjourned. I would like to thank the witnesses for their testimony and for their responses to the questions. Thank you.

[Whereupon, at 12:18 p.m., the hearing was adjourned.]

A P P E N D I X

June 18, 2013

Testimony of Michael D. Calhoun
President, Center for Responsible Lending

Before the House Committee on Financial Services
Subcommittee on Financial Institutions and Consumer Credit

June 18, 2013

Good Morning Chairman Capito, Ranking Member Meeks, and Members of the Subcommittee. Thank you for inviting me to testify at today's hearing to discuss the Consumer Financial Protection Bureau's implementation of mortgage reforms that will prevent future lending abuses and promote stability in the mortgage market.

I am President of the Center for Responsible Lending (CRL), a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, a nonprofit community development financial institution. For thirty years, Self-Help has focused on creating asset-building opportunities for low-income, rural, women-headed, and minority families, primarily through financing safe, affordable home loans and small business loans. In total, Self-Help has provided $6 billion in financing to 70,000 homebuyers, small businesses and nonprofit organizations and serves more than 80,000 mostly low-income families through 30 retail credit union branches in North Carolina, California, and Chicago.

The Consumer Financial Protection Bureau (CFPB) has released mortgage rules that strike the right balance of protecting consumers while also enabling lenders to comply with these new reforms. Throughout the rulemaking process and in the final result, the CFPB has taken a measured and reasonable approach. As a result, these mortgage rules will provide important legal protections for borrowers and for lenders.

The rules—required by the Dodd-Frank Act of 2010—address head-on a key cause of the mortgage meltdown and ensuing recession: many lenders made high-risk, often deceptively packaged home loans without assessing if borrowers could repay them. Because of these reforms, lenders now must assess a mortgage borrower's ability to repay a loan. The rules' definition of a safe mortgage—known in Dodd-Frank as a "Qualified Mortgage"— also means that restrictions on harmful loan terms such as balloon payments, teaser rates and high fees will extend to families who in the past too often were steered into unfair, harmful financial products. At the same time, the CFPB's rule provides lenders with significant legal protection when they originate Qualified Mortgages, although they are not required to do so.

In assessing the CFPB's Qualified Mortgage definition, my testimony will highlight the same "scorecard" of issues that CRL highlighted in front of this subcommittee at a hearing last summer before the CFPB issued its final rules:

- **Qualified Mortgage definition is broadly defined:** The CFPB's rules adopt the widespread view – including from CRL – that Qualified Mortgages should be broadly defined to encompass the vast majority of the current mortgage market. The rules include four different paths for a mortgage to gain QM status, including one specifically for small creditors holding loans in portfolio and another one that is based on eligibility for purchase or insurance by Fannie Mae, Freddie Mac and the Federal Housing Administration. This multi-faceted approach will maintain access to affordable credit for borrowers.

- **The CFPB used clear, bright lines in the Qualified Mortgage definition:** In addition, the CFPB used specific standards to define which mortgages will be eligible to obtain QM status. The CFPB's first prong for a Qualified Mortgage definition uses a back-end debt-to-income ratio cut-off of 43 percent, and another definition depend on whether the loan is eligible for purchase or insurance by well-established programs. This specificity will enable both lenders and borrowers to know upfront when a mortgage is originated whether it has QM status.

- **Qualified Mortgage definition protects borrowers with the riskiest loans:** On the issue of whether lenders should receive a safe harbor or a rebuttable presumption of compliance when originating a QM loan, the CFPB created a two-tier system. The vast majority of loans will have a safe harbor and others will have a rebuttable presumption. The threshold between the two depends on the loan's annual percentage rate (APR) relative to the average prime offer rate (APOR). Ideally, as consumer groups supported, the new rules would have allowed any borrower with a QM loan to challenge a lender who failed to evaluate if the borrower could afford the loan. However, the CFPB's rules do allow borrowers to hold lenders accountable on the riskiest types of mortgages, those in the subprime market where the problems that led to the housing crisis were concentrated.

As a whole, these rules continue the CFPB's approach of expanding access to credit while ensuring that loans are sustainable for the borrower, the lender and the overall economy.

I. Harmful Mortgage Features and Lending Practices Were Prevalent in the Pre-Crisis Mortgage Lending Market and Led to Massive Foreclosures.

In the fallout of the foreclosure crisis, the alphabet soup of harmful lending products and practices – such as YSPs, IOs and NINJA loans – is now well known. Many of these features and practices were at one time touted as innovations to serve borrowers. As the foreclosure crisis has made plain, such rhetoric has failed to match reality.

For more than ten years, CRL has produced research highlighting the increased foreclosure risk posed by abusive lending practices. In 2006, which pre-dated the worst of the foreclosure crisis, CRL released a report estimating that abusive and predatory lending would lead to approximately 2.2 million foreclosures among subprime mortgages.[1] At the time, our report was denounced by the mortgage industry as absurdly pessimistic. As we all now know, the system was loaded with much more risk than CRL originally reported.

CRL released a follow-up report entitled *Lost Ground* in 2011 that builds on our pre-crisis research and confirms the link between risky mortgage features and foreclosure rates. For mortgages originated between 2004 and 2008, this research shows that loans originated by a mortgage broker, containing hybrid or option ARMs, having prepayment penalties, and featuring high interest rates (i.e., subprime loans) were all significantly more likely to be seriously delinquent or foreclosed upon than a 30-year fixed-rate mortgage without a prepayment penalty.[2]

CRL's research also demonstrates that African-American and Latino borrowers were much more likely to receive mortgages with these risky features. For example, African-American and Latino borrowers with FICO scores above 660 were **three times** as likely

[1] *See* Ellen Schloemer, Wei Li, Keith Ernst, and Kathleen Keest, *Losing Ground: Foreclosures in the Subprime Market and Their Costs to Homeowners*, (December 2006), available at http://www.responsiblelending.org/mortgage-lending/research-analysis/foreclosure-paper-report-2-17.pdf.

[2] *See* Debbie Gruenstein Bocian, Wei Li, Roberto Quercia, *Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosures*, (November 2011), available at http://www.responsiblelending.org/mortgage-lending/research-analysis/Lost-Ground-2011.pdf.

to have a higher interest rate mortgage than white borrowers in the same credit range.[3] Although the majority of foreclosures have affected white borrowers, *Lost Ground* confirms that African-American and Latino borrowers have faced a disproportionate number of foreclosures and delinquencies than white borrowers within every income range.

The foreclosure crisis could have been prevented, but it wasn't, and it bears revisiting the kind of harmful lending practices that fueled the crisis still affecting communities across the country.

- **2/28s and other ARMs:** Adjustable rate mortgages (ARMs) – including "2/28s" where starter rates reset after the first two years – were widespread in the years leading up to the foreclosure crisis. These 2/28s and other ARMs led to payment shocks for many households who were unprepared for higher monthly payments once the interest rates increased. As of 2009, subprime mortgages with short-term hybrid ARMs had serious delinquency rates of 48 percent compared to 21 percent for subprime fixed-rate mortgages and 36 percent for the total universe of active subprime mortgages.[4] In fact, were it not for the Federal Reserve lowering interest rates to historically low levels following the financial crisis, it's easy to imagine the payment shock from expiring teaser rates leading to an even higher number of foreclosures than has occurred so far.

  A related product called interest-only (IO) ARMs let borrowers make interest only payments during an introductory period, which jeopardized any ability to build equity as well as leading to payment shock for borrowers once the loan started amortizing over a reduced loan life. Going even further, payment option ARMs (POARMs) allowed borrowers to make monthly payments where the amount paid could vary from month-to-month, including payment amounts that did not cover the full interest due. This resulted in negative amortization. Too many lenders structured these loans so that the payments would substantially increase in five years or less when borrowers hit their negative amortization cap, underwrote the loans only to the very low introductory teaser rate, and failed to document income.

- **Prepayment penalties:** Many borrowers facing payment shock from increased interest rates once an introductory period ended also faced penalties when trying

[3] *Id.*
[4] *See* GAO Nonprime Mortgages: Analysis of Loan Performance, Factors Associated with Defaults, and Data Sources, at 12-13 (August 2010) (available at http://www.gao.gov/assets/310/308845.pdf).

to exit into a new mortgage or to sell the property to avoid these built-in increases. These prepayment penalties are a feature associated with a higher likelihood of default[5] and were present in the great majority of subprime mortgages, and increasingly in Alt-A mortgages (which generally consisted of limited documentation mortgages to higher credit score borrowers), during the mortgage boom.[6] To avoid default, the typical subprime borrower had to sell or refinance before the rate reset. This produced prepayment penalties, generally equal to six months' interest— typically 3.5 percent to 4 percent of the loan balance. Because the average borrower did not have the cash on hand sufficient to cover the prepayment penalties and refinancing fees, they had to pay them from the proceeds of the new loan. This produced ever-declining equity even when home prices were rising. Once home prices declined, foreclosure risk climbed catastrophically.

- **No-doc or low-doc loans:** The practice of failing to document a borrower's income and assets was also prevalent in the subprime and Alt-A market. For example, low-doc loans comprised 52 percent of Alt-A originations in April 2004 and rose to 78 percent at the end of 2006.[7] By 2006, no-doc or low-doc loans made up *27% of **all** mortgages*.[8] These loans without proper documentation were frequently underwritten with inflated statements of the borrower's income.[9] Lawyers representing borrowers in predatory lending cases often found the borrower's tax returns included in the file of those who were nevertheless given "no doc" or "low doc" loans. Unbeknownst to these borrowers, they paid higher interests rate for the "privilege" of receiving a no-

[5] *See, e.g.*, Lei Ding, Roberto G. Quercia, Wei Li, Janneke Ratcliffe, *Risky Borrowers or Risky Mortgages: Disaggregating Effects Using Propensity Score Models*, at 49 (Working Paper: May 17, 2010) (stating "[w]e also found that subprime loans with adjustable rates have a significantly higher default rate than comparable CAP loans. And when the adjustable rate term is combined with the prepayment-penalty feature, the default risk of subprime loans becomes even higher.") (available at http://www.ccc.unc.edu/documents/Risky.Disaggreg.5.17.10.pdf).

[6] *See Report to Congress on the Root Causes of the Foreclosure Crisis*, U.S. Department of Housing and Urban Development, Office of Policy Development and Research, at 23 (January 2010) (citing Demyanyk, Yuliya, and Otto Van Hemert. 2008. Understanding the Subprime Crisis. Working paper. St. Louis, MO: Federal Reserve Bank of St. Louis.) (available at http://www.huduser.org/Publications/PDF/Foreclosure_09.pdf).

[7] Rajdeep Sengupta, *Atl-A: The Forgotten Segment of the Mortgage Market*, Federal Reserve Bank of St. Louis Review, January/February 2010, 92(1), pp. 55-71 at 60 (available at http://research.stlouisfed.org/publications/review/10/01/Sengupta.pdf).

[8] *See* Financial Crisis Inquiry Commission, *Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States*, at 165 (Jan. 2011) [hereinafter FCIC Report], (available at http://fcicstatic.law.stanford.edu/cdn_media/fcic-reports/fcic_final_report_full.pdf).

[9] Over ninety percent of a sample of stated income loans exaggerated income by 5 percent or more and almost 60 percent exaggerated income by over 50 percent. Mortgage Asset Research Institute, Inc, Eighth Periodic Mortgage Fraud Case Report to Mortgage Bankers Association at 12 (April 2006), (available at http://www.mortgagebankers.org/files/News/InternalResource/42175_Final-8thAnnualCaseReporttoMBA.pdf).

doc loan, even where they provided full documentation to the broker.

- **Yield Spread Premiums:** The proliferation of mortgages with these harmful features was driven in significant part by the use of yield spread premiums (YSPs) as a way to compensate mortgage brokers. Because YSPs paid mortgage brokers higher payments when a mortgage had a higher interest rate than the borrower qualified for, these YSPs gave mortgage brokers incentives to steer borrowers into loans that were more expensive and less stable than they qualified for. And, by 2006, mortgage brokers accounted for 45 percent of all mortgage originations and 71 percent of all non-prime mortgage originations.[10] In fact, most borrowers who received subprime loans could have qualified for better, more sustainable loans. Many qualified for lower-cost prime loans;[11] those who did not often would have qualified for sustainable, 30-year fixed-rate subprime loans for at most 50-80 basis points above the introductory rate on the unsustainable "exploding" ARM loans they were given.[12] This 50-80 basis point increase is modest compared with the 350 to 400 basis point prepayment penalty (plus additional refinancing fees) that the borrower had to pay to refinance the typical 2/28 loan before the end of the second year.

- **No Escrows for Taxes and Insurance:** Subprime lenders commonly did not escrow for taxes and insurance, attracting borrowers with the deceptive lure of lower monthly payments. This practice increased the risk of default twice a year when the tax and insurance bills came due and produced further equity-stripping cash-out refinancings where the borrower had the equity to cover the bills and refinancing fees and penalties.

On top of these harmful loan features and lending practices, many lenders also failed to determine whether a borrower had an actual ability to repay their mortgage. Proper

[10] Ren S. Essene & William Apgar, *Understanding Mortgage Market Behavior: Creating Good Mortgage Options for All Americans*, at 8 (Joint Center for Housing Studies, Harvard University Apr. 25, 2007) (citing Mortgage Bankers Association, MBA Research Data Notes: Residential Mortgage Origination Channels (2006) (available at http://www.jchs.harvard.edu/sites/jchs.harvard.edu/files/mm07-1_mortgage_market_behavior.pdf).

[11] For example, a Wall Street Journal study found that 61 percent of the subprime loans originated in 2006 that were packaged into securities and sold to investors "went to people with credit scores high enough to often qualify for conventional [i.e., prime] loans with far better terms." *See* Rick Brooks & Ruth Simon, *Subprime Debacle Traps Even Very Credit-Worthy As Housing Boomed, Industry Pushed Loans To a Broader Market*, Wall Street Journal at A1 (Dec 3, 2007). Freddie Mac estimated in 2005 that more than 20 percent of borrowers with subprime loans could have qualified for prime. *See* Mike Hudson & E. Scott Reckard, *More Homeowners With Good Credit Getting Stuck With Higher-Rate Loans*, Los Angeles Times (Oct. 25, 2005), available at http://articles.latimes.com/2005/oct/24/business/fi-subprime24.

[12] January 25, 2007 letter from the Coalition for Fair and Affordable Lending ("CFAL") to Ben S. Bernanke, Sheila C. Bair, John C. Dugan, John M. Reich, JoAnn Johnson, and Neil Milner, at 3. CFAL was an industry group representing subprime lenders.

underwriting is particularly important for mortgages with resetting interest rates or negative amortization or interest-only payments (or all of the above) to ensure that borrowers can afford the larger monthly payments when they kick in down the road. However, for many mortgage lenders, this straightforward underwriting never happened. For example, at the time when Federal regulators proposed that lenders fully underwrite mortgages with ARMs, interest-only and negative amortization features at the fully indexed rate and payment, Countrywide estimated that 70% of their recent borrowers would be unable to meet this standard.[13] This recklessness set borrowers up for failure and, as a result, caused a foreclosure crisis.

The CFPB's rules implementing the Ability to Repay and Qualified Mortgage reforms put in place a system of incentives that will make it difficult for this kind of risky lending to re-emerge in the mortgage market. Overall, these incentives work in two ways. First, while lenders are not required to originate QM loans, they receive a legal presumption of meeting the separate obligation to reasonably determine that a borrower can afford the offered mortgage. Second, QM loans benefit borrowers, because these mortgages are restricted from having many of the risky product features that fueled the subprime lending crisis. The CFPB's Qualified Mortgage definition is explored in more detail below.

II. Overview of the CFPB's Rulemakings on the Qualified Mortgage Definition.

After an extensive rulemaking process that included the Federal Reserve proposing a rule in 2011 and the CFPB seeking additional notice and comment in 2012, the CFPB has released two rulemakings on the Qualified Mortgage definition this year. The CFPB released its first rulemaking on January 10, 2013.[14] On the same day, the CFPB released a concurrent proposal to obtain additional comment on additional aspects of the definition. These remaining pieces of the definition were finalized in a rulemaking released on May 29, 2013.[15] As part of its implementation process and in response to stakeholder

[13] Countrywide Financial Corporation, "3Q 2007 Earnings Supplemental Presentation," Oct. 26, 2007.
[14] Consumer Financial Protection Bureau, Ability to Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6408 (January 30, 2013) (rule was issued by the CFPB on January 10, 2013 and printed in the Federal Register on January 30, 2013) (hereinafter "January 2013 Final Qualified Mortgage Rule").
[15] Consumer Financial Protection Bureau, Ability to Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 34430 (June 12, 2013) (rule was issued by the CFPB on May 29, 2013 and printed in the Federal Register on June 12, 2013) (hereinafter "May 2013 Final Qualified Mortgage Rule").

feedback, the CFPB has also published notices requesting comment on ways to clarify the rules and provide further guidance.

Throughout the rulemaking process – including the implementation efforts – the CFPB has sought extensive feedback from various stakeholders and has incorporated that feedback into the final rules. The result is a rule that reigns in many of the risky product features and lending practices that harmed borrowers during the subprime lending crisis while also prioritizing access to credit in many of the ways sought by lenders.

A. Overview of Qualified Mortgage Definition.

In order to create a rule that meets consumer protection goals while also providing flexibility, the CFPB has established four different paths for loans to gain QM status. Each are detailed below:

- **General Definition:** The general Qualified Mortgage definition requires eligible loans to not exceed the points and fees threshold, not have negative amortization or interest-only payments, and a term that does not exceed 30 years. In addition, borrowers must have a back-end debt-to-income ratio at 43% or below. Lenders must collect and verify a borrower's income, assets, debts and other obligations according to standards established in the regulation, which are found in Appendix Q of the regulation, in order to calculate the borrower's debt-to-income ratio.

- **Compensating Factors:** The CFPB also created a temporary definition that allows loans eligible for insurance or guarantee by Fannie Mae, Freddie Mac, the Federal Housing Administration (FHA), the Rural Housing Service (RHS), and the Veterans Administration (VA) to gain Qualified Mortgage status. The CFPB created the temporary QM definition in order to "preserve[] access to credit in today's market by permitting a loan that does not satisfy the 43 percent debt-to-income ratio threshold to nonetheless be a qualified mortgage based upon an underwriting determination made pursuant to guidelines created by the GSEs while in conservatorship or one of the Federal agencies."[16] These agency guidelines include additional underwriting standards – often called "compensating factors" – in order to approve a borrower with a debt-to-income ratio above 43 percent.

  This temporary definition is available for a maximum of seven years; however, there are situations where elements of the definition could expire sooner for each

[16] January 2013 Final Qualified Mortgage Rule, at 6506.

of the individual programs. Under the Dodd-Frank Act, the FHA, RHS and VA can issue their own rulemakings defining Qualified Mortgages for the respective agency program, and the CFPB's temporary designation for that agency would expire if and when that occurs. Additionally, the temporary definition for Fannie Mae and Freddie Mac guaranteed loans would also expire if the GSEs exit conservatorship by the Federal Housing Finance Agency (FHFA) before the seven-year period ends. This temporary definition does not require that the GSEs or government agencies actually insure or guarantee loans under this category – only that loans would be eligible under the specified underwriting requirements for one of the GSEs or government agencies.

- **Portfolio Loans Originated by Small Creditors Definition:** This definition is not required in the Dodd-Frank Act, but the CFPB created this designation using its regulatory authority with the goal of preserving access to credit. Under this definition, lenders need to meet two criteria to count as a small creditor: first, have assets of no more than $2 billion and second, originate no more than 500 first-lien mortgages per year. Mortgages originated by an eligible small creditor can obtain QM status if they meet the points and fees threshold, there is no negative amortization, no interest-only payments, and the loan has a term of no more than 30 years. In addition, the lender is also "required to consider the consumer's debt-to-income ratio or residual income and to verify the underlying information."[17] However, borrowers do not need to meet the 43% debt-to-income ratio threshold or use the debt-to-income ratio standards in Appendix Q.

- **Balloon-Loan Definition:** The CFPB also created a Qualified Mortgage definition specific to balloon loans. This designation is required by the Dodd-Frank Act, but the CFPB also used its regulatory authority to establish a two-year transition period that allows all small creditors – regardless of whether they operate in rural or underserved areas – to obtain QM status for balloon loans that are held in portfolio. After the transition period, the balloon loan definition only applies to those lenders who operate in rural or underserved areas under a definition that CFPB will continue to study. Both during the transition period and afterwards, balloon loans must meet the points and fees threshold, have no negative amortization, "have a term of at least five years, a fixed-interest rate, and meet certain basic underwriting standards; debt-to-income ratios must also be considered but are not subject to the 43 percent general requirement."[18]

[17] May 2013 Final Qualified Mortgage Rule, at 35487.
[18] January 2013 Final Qualified Mortgage Rule, rule at 6409.

An aspect of the QM definition that is consistent across all four of these categories is the requirement that loans not exceed the points and fees thresholds established by the CFPB. The points and fees definition established by the CFPB is addressed in the next subsection.

B. The Qualified Mortgage Points and Fees Threshold Prevents a Return to High Fee Lending While Also Facilitating Lender Compliance.

One borrower protection included across the four Qualified Mortgage definitions is a limit on the amount of points and fees the loan can have. Points are another name for upfront fees paid by the borrower, which encompass a number of items including yield spread premiums, origination fees and discount points. These costs are often expressed as a percentage of the borrower's loan amount where one point is equal to one percent of the loan amount. The points and fees component of the Qualified Mortgage definition ensures that higher fee loans – where lenders and originators would have less of an incentive to determine that a borrower has an ability to repay the loan over time because they receive so much compensation up-front – cannot benefit from the liability protections that come with QM status.

The statutory language in the Dodd-Frank Act states that the points and fees cannot exceed 3% of the loan balance, but there are other provisions in the statute and CFPB's rules that make this threshold larger than just 3% in practice. First, the Qualified Mortgage rules allow lenders to exclude up to two bona fide discount points that reduce the interest rate the borrower pays from the overall points and fees calculation. Second, fees paid by the borrower to independent third-parties are not included in the definition. Both of these exceptions allow for a substantial increase in the amount of fees a borrower can pay and still have the loan considered a QM. Third, the CFPB's rule also accommodates smaller loans by having higher points and fees thresholds for loans under $100,000. Only loan amounts of $100,000 or more have a points and fees threshold of 3%, and the CFPB set the below thresholds for smaller mortgages:

- **3%:** loan balance is $100,000 and above (i.e., $6,000 for a $200,000 loan)
- **$3,000:** loan balance is greater than or equal to $60,000 and less than $100,000
- **5%:** loan balance is greater than or equal to $20,000 and less than $60,000
- **$1,000:** loan balance is greater than or equal to $12,500 and less than $20,000
- **8%:** loan balance is less than $12,500

Three parts of the points and fees definition – loan originator compensation (including yield spread premiums), settlement services paid to companies affiliated with the lender, and loan level price adjustments – are addressed in greater detail below.

1. Yield spread premiums are included the points and fees definition, but commissions to individual retail and mortgage broker loan officers are excluded.

The CFPB has closely considered the issue of how to count loan originator compensation in the definition of points and fees, and the final regulations issued on May 29, 2013 address this issue in detail. In this final rule the CFPB requires including all yield spread premiums (YSPs) in the points and fees definition, plus any upfront payment that borrowers pay directly to lenders and mortgage brokers. YSPs are the payments that lenders make to mortgage brokers, which are indirectly funded by the borrower through an increased interest rate. In addition, the CFPB used its exception authority to exclude all commissions paid to individual mortgage broker and retail loan officers from the points and fees definition.

The inclusion of YSPs in the points and fees definition is a significant reform that will help prevent a return to the kind of abusive lending practices that dominated during the subprime lending boom. Prior to passage of the Dodd-Frank Act, YSPs were not included in the definition of points and fees used to calculate whether a loan counted as a high-cost HOEPA loan. The Dodd-Frank Act amended this definition to include YSPs, and the CFPB's regulations have implemented this reform. This is an appropriate change, because the underlying premise of a YSP is that it allows the borrower to pay a mortgage broker through an increased interest rate as a substitute for compensating the mortgage broker in cash up-front.[19]

Since YSPs and upfront payments are direct alternatives for one another, these payments must count equally in the points and fees definition. As a result, a loan with 1.75% paid by the borrower to the brokerage upfront will be treated the same as a loan with 1.75% paid by the lender to the brokerage.

If the CFPB had, instead, chosen to fully or partially exclude YSPs from the points and fees definition, this would have created an improper incentive for originators to use YSPs instead of upfront payments paid directly by the borrower. Such a structure would result in less transparent transactions that make it harder for consumers to comparison-shop and, and a result, often result in higher cost transactions.

While other reforms in the Dodd-Frank Act also aim to curb steering abuses, the points and fees limit is an essential reform to prevent a return to high fee lending. Because mortgage brokers are independent businesses (and not employees of the creditor), they can choose which lenders to do business with and can base this decision on who pays the

[19] *See Nat'l Assoc. of Mortgage Brokers v. Fed. Reserve Bd.*, 773 F.Supp. 2d 151, 158 (D.D.C 2011).

highest YSP compensation. Lenders must compete for broker business, and they compete by bidding up payments to brokers, which inflates broker payments through reverse competition. Some brokers specialize in offering subprime loans that generated the greatest compensation. Prohibitions on loan term-based compensation would not prohibit such a result, as the DC District Court concluded in upholding the Federal Reserve's originator compensation rules.[20] Additionally, anti-steering rules do not require brokers to develop business relationships with lower cost lenders. Counting YSPs in points and fees is a necessary counterweight to this continued ability for brokers to steer borrowers into loans that benefit the brokers more than the borrowers.

The CFPB's May 29th rulemaking also provided that all commissions paid by mortgage brokers or retail lenders to their respective individual employee loan officers are excluded from the points and fees definition. The CFPB interpreted the statutory language as including these payments in the definition of points and fees, but the agency used its rulemaking authority to exclude them. The CFPB had proposed to exempt payments by mortgage broker companies to their employees because of concerns about double counting the compensation paid to the mortgage broker company by the borrower or the lender but had not proposed to exempt payments by retail lenders to their employee loan officers. In the May 29, 2013 rule, however, the CFPB decided to treat employees of both types of entities the same because "there were significant operational challenges to calculating individual employee compensation accurately early in the loan origination process, and that those challenges would lead to anomalous results for consumers. In addition, the Bureau concluded that structural differences between the retail and wholesale channels lessened risks to consumers."[21] CRL supports this decision by the CFPB.

2. Settlement services provided by companies affiliated with the lender are included in the points and fees definition.

In conformance with the statutory language in place since HOEPA was first passed in 1994, the CFPB's rulemakings also established that settlement services provided by

[20] In upholding the Federal Reserve's 2010 loan originator compensation rule, the District Court noted that the prohibition on term-based compensation by itself did not eliminate all incentives for abuse by mortgage brokers: "Thus, proposed regulation § 226.36(d)(1), which prevents any compensation model based on the terms of the transaction, by itself, ensures that creditors' employees have no direct monetary incentive to direct consumers toward loans with higher rates of more adverse terms. ... The same is not true, however, for mortgage brokers. Although § 226.36(d)(1) prevents mortgage brokers from receiving compensation tied to the terms of a loan, it does not prevent them or their employees from creating incentives for a loan officer to guide consumers toward certain loans and or to certain lenders." *See Nat'l Ass'n of Mortgage Brokers*, 773 F.Supp.2d at 175.

[21] May 2013 Final Qualified Mortgage Rule, at 35430.

companies affiliated with the lender are included in the points and fees definition. Some settlement service providers – such as companies that provide title insurance – are affiliated with lenders, while others are independent and unaffiliated with any individual lender. It has been reported that 74% of the market uses unaffiliated providers. Because one of the underlying purposes of the QM points and fees definition is to include all compensation received by the lender, the QM points and fees definition differentiates between service providers that are affiliated with a lender and those that are not. Accordingly, if a title insurer is affiliated with the lender used by the borrower, then the fees paid by the borrower for that title insurance are included in the points and fees calculation.

Title insurance, which is one type of settlement service, is included in most mortgage transactions, but borrowers typically have limited control over the price charged for this service. A 2007 report by the U.S. Government Accountability Office found that "because consumers generally do not pick their title agent or insurer, title agents do not market to them but to the real estate and mortgage professionals who generally make the decision."[22] As a result, the GAO concluded that borrowers end up "in a potentially vulnerable situation where, to a great extent, they have little or no influence over the price of title insurance but have little choice but to purchase it."[23]

Given this market dynamic where borrowers overpay for title insurance because businesses are competing to drive up prices instead of driving them down, the points and fees definition provides needed pressure to reduce these costs for borrowers. Including title insurance costs in the points and fees definition where the lender has an affiliation with the company supplying the title insurance reasonably targets the transactions with the most potential for up-charging.

3. Loan Level Price Adjustments are included in the points and fees definition.

On the issue of Loan Level Price Adjustments (LLPAs), the CFPB's regulation determined to not create an exemption for these charges out of concern that it would disadvantage smaller lenders that held loans in portfolio. Fannie Mae and Freddie Mac use LLPAs to price loans they determine to have a higher risk, and these LLPAs result in a fixed fee for mortgages with specified characteristics.[24] For example, Fannie Mae and

[22] *Title Insurance: Actions Needed to Improve Oversight of the Title Insurance Industry and Better Protect Consumers*, United States Government Accountability Office, GAO-07-401 (April 2007).
[23] *Id.*
[24] Fannie Mae, Loan-Level Price Adjustment (LLPA) Matrix and Adverse Market Delivery Charge (AMDC) Information, (September 20, 2012) (available at https://www.fanniemae.com/content/pricing/llpa-

Freddie Mac have an LLPA of 0.75% (75 basis points) for mortgages to purchase a condominium where the down payment is less than 25%. In evaluating comments arguing that these charges should be excluded from the points and fees definition, the CFPB concluded that the way Fannie Mae and Freddie Mac use LLPAs "is better viewed as a fundamental component of how the pricing of a mortgage loan is determined rather than a third party charge."[25] As a result, the CFPB found that "allowing creditors to exclude points charged to offset LLPAs could create market imbalances between loan sold on the secondary market and loans held in portfolio."[26] In other words, allowing this exception would give some loans – but not others – a type of discount in how they price the riskiness of a loan. If the LLPA is, as is generally the case, paid for through a higher interest rate rather than in points and fees up-front, they are not counted under the CFPB's rules.

III. Qualified Mortgage Definition and Future Mortgage Lending.

Taken as a whole, the CFPB's rules for the Qualified Mortgage definition are a reasonable approach to implement the reforms in the Dodd-Frank Act. In reaching this assessment, CRL looks to three different factors: 1) whether QM is defined broadly, 2) whether the definition uses clear, bright line standards, and 3) whether it provides borrowers with the ability to raise a challenge when a lender failed to reasonably determine whether the borrower could afford the offered mortgage.

A. Qualified Mortgage Definition is Broadly Defined.

The CFPB has drafted a QM rule that will cover the vast majority of the current mortgage market. This will prevent a dual mortgage market from developing, because a broad range of families capable of owning a home – including lower-income borrowers and borrowers of color – will be able to take advantage of mainstream Qualified Mortgages that are restricted from having risky product features instead of being pushed into more expensive loans with abusive features and high fees.

The breadth of the CFPB's rule is evident when considering that the Bureau adopted four different ways that a loan can gain Qualified Mortgage status. Among these is the definition relying on whether a loan is eligible to be guaranteed or insured by Fannie

matrix.pdf); Freddie Mac, Single-Family Seller/Servicer Guide, Exhibit 19: Postsettlement Delivery Fees (September 14, 2012) (available at http://www.freddiemac.com/singlefamily/pdf/ex19.pdf).
[25] January 2013 Final Qualified Mortgage Rule, at 6430.
[26] *Id.*

Mae, Freddie Mac or a government agency program. This definition incorporates the compensating factors used by the GSEs or government agencies in order to lend to borrowers with debt-to-income ratios above 43%. The CFPB designed the rule in this way to "help ensure access to responsible, affordable credit is available for consumers with debt-to-income ratios above 43 percent and facilitate compliance by creditors by promoting the use of widely recognized, federally-related underwriting standards."[27] Since loans guaranteed by Fannie Mae and Freddie Mac and insured by FHA and other government programs constitute approximately 90% of the current mortgage market, this definition on its own will cover the overwhelming majority of future mortgage lending.

In addition to covering current mortgage lending, the CFPB's rule also has the potential to bring additional private capital into the market. As described in the CFPB's rulemaking, "[t]he temporary exception has been carefully structured to cover loans that are eligible to be purchased, guaranteed, or insured by the GSEs (while in conservatorship) or Federal agencies regardless of whether the loans are actually so purchased, guaranteed, or insured; this will leave room for private investors to return to the market and secure the same legal protection as the GSEs and Federal agencies."[28] For example, if a private investor securitizes loans according to the standards in Desktop Underwriter – which adheres to Fannie Mae's underwriting guidelines – then these loans can obtain QM status even though they are not sold to the GSEs.

Lastly, the definition focused on smaller creditors holding loans in portfolio also provides flexibility for these lenders to exceed the 43% debt-to-income ratio cutoff that is the CFPB's general definition. In its rulemaking, the CFPB addressed the aligned incentives that small creditors holding loans in portfolio generally have to make affordable loans to borrowers:

> Small creditors also have particularly strong incentives to make careful assessments of a consumer's ability to repay because small creditors bear the risk of default associated with loans held in portfolio and because each loan represents a proportionally greater risk to a small creditor than to a larger one. In addition, small creditors operating in limited geographical areas may face significant risk of harm to their reputations within their communities if they make loans that consumers cannot repay.[29]

As a result of these aligned incentives and concerns that smaller lenders might restrict their lending if required to comply only with the general definition that has a 43% debt-

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[27] *Id.*, at 6533.
[28] *Id.*, at 6534.
[29] May 2013 Final Qualified Mortgage Rule, at 35485.

to-income ratio threshold, the CFPB concluded that creating a separate definition tailored to these lenders was appropriate. The CFPB concluded that "[b]ecause there are thousands of small creditors as defined by § 1026.43(e)(5) in the United States, the Bureau believes that § 1026.43(e)(5) is likely to preserve access to affordable, responsible mortgage credit for hundreds of thousands of consumers annually."[30] These definitions, as a whole, demonstrate that the CFPB's rules not only cover the vast majority of the current market, but will also provide flexibility for mortgage lending moving forward.

Two additional points bear mentioning in terms of the breadth of the CFPB's definition. First, it's important to put CoreLogic's analysis of the Qualified Mortgage rule conducted earlier this year in proper context, because CoreLogic's conclusions are often taken out of context and faulty assumptions in their methodology are often not mentioned. CoreLogic's analysis found that when factoring in the definition relying on eligibility for guarantee or insurance by Fannie Mae, Freddie Mac, and the government agencies, "the near- and intermediate-term impacts of the rule are **very small**."[31] When assessing the general definition that uses a 43% debt-to-income ratio cutoff, the CoreLogic analysis claims that 52% of 2010 originations would be covered by this definition. However, CoreLogic made several unnecessary assumptions resulting in an overly conservative analysis. First, it excludes all loans with credit scores below 640, although the Qualified Mortgage definition does not impose any credit score requirements. Second, it assumes that borrowers who received loan products with prohibited features would not be able to access QM-eligible loan products in the future – in fact, borrowers will be able to get safer mortgages instead. Unfortunately, this 52% figure is often taken out of context (i.e., the eligible for guarantee or insurance prong of the Qualified Mortgage definition is ignored) and the weaknesses in their assumptions are not mentioned.

Second, while there is limited data on the amount of points and fees charged to borrowers in recent years, it is clear that the vast majority of recent mortgages would not exceed the points and fees thresholds required under the QM definition. As described earlier, the statutory points and fees definition excludes a number of origination costs from being counted in points and fees, such as upfront mortgage insurance premiums, up to two bona fide discount points, third party closing costs, and commissions paid to individual loan officers employed by mortgage broker and retail companies.

Of the remaining charges eligible to be included in the points and fees definition, several sources confirm that the origination charges paid directly to lenders constitute a small

[30] *Id.*

[31] Sam Khater, *The Mortgage Market Impact of Qualified Mortgage Definition*, CoreLogic, The MarketPulse, Volume 2, Issue 2 (February 12, 2013)(available at http://www.corelogic.com/downloadable-docs/MarketPulse_2013-February.pdf) (emphasis added).

percentage of overall loan balances. Freddie Mac provides weekly reports on the average fees charged to borrowers, and the figure for the week of June 13, 2013 was 0.7%, well under the 3% limit.[32] This figure is confirmed by an industry comment filed with the CFPB, which also finds that the origination charges paid by borrowers (up-front points and fees and more than two discount points) were – for all loan sizes – less than 1%.[33]

This leaves considerable room in the points and fees calculation for other possible fees, such as mortgage broker compensation and settlement services paid to a company affiliated with the lender. The industry comment mentioned above determines that if **all** settlement services are provided by companies affiliated with the lender for every loan in the sample, then 5.6% of all loans would exceed the points and fees limit. However, not all lenders use affiliated settlement service providers; the Mortgage Bankers Association reports that there is 26% market share for affiliated settlement service providers.[34] As a result, it's appropriate to discount the comment's estimates by 74%, since loan level data on this sample is not available. This would result in 1.46% of all loans in the study sample exceeding the points and fees threshold when taking affiliate service providers into account, meaning that practically 99% of all loans in this sample would meet the QM points and fees limits. And, even this 99% figure is understated, because any of these remaining loans could meet the points and fees limit by using settlement service providers that are not affiliated with the lender, as most loans do, or by financing some of the fees into the interest rate.

B. The CFPB Used Clear, Bright Lines in the Qualified Mortgage Definition.

In addition to providing a broad QM definition, the CFPB also used clear, bright lines in establishing all four of the QM definitions. For example, the first prong of CFPB's definition for a QM loan includes a back-end debt-to-income ratio cut-off of 43% as one element of the definition. In establishing this threshold, the CFPB noted that that using a specific debt-to-income ratio cutoff "provides a well-established and well-understood rule that will provide certainty for creditors and help to minimize the potential for disputes and costly litigation over whether a mortgage is a qualified mortgage."[35] The CFPB also pointed to the fact that "[a] specific debt-to-income ratio threshold also provides additional certainty to assignees and investors in the secondary market, which

[32] Freddie Mac, Weekly Primary Mortgage Market Survey (PMMS) (available at http://www.freddiemac.com/pmms/).
[33] AB Schnare Associates LLC, Ex Parte Comment on CFPB-2013-002, at 5 (April 5, 2013) (available at http://www.regulations.gov/#!documentDetail;D=CFPB-2013-0002-0933.).
[34] Mortgage Bankers Association, *Ensuring Housing Recovery: The Challenge of the Ability to Repay and Qualified Mortgage Rule to Credit Availability and Affordability for Homeowners*, at 18 (February 28, 2012) (available at http://www.fdic.gov/regulations/reform/MBA2-28-12.pdf).
[35] January 2013 Final Qualified Mortgage Rule, at 6505-06.

should help reduce possible concerns regarding legal risk and potentially promote credit availability."[36] Additionally, the CFPB's definition relying on whether the loan is eligible for purchase or insurance by well-established programs also results in clear, bright line standards.

The CFPB's final rules provide substantial clarity on these definitions, which will enable both lenders and borrowers to know upfront when a mortgage is originated whether it has QM status. Furthermore, the CFPB is also working to refine and clarify these definitions through their implementation process. This includes publishing further guidance to clarify issues such as how requested put-backs on Fannie Mae, Freddie Mac and government agency mortgages will impact Qualified Mortgage status.

C. Qualified Mortgage Definition Protects Borrowers with the Riskiest Loans.

Leading up to the CFPB's final rule in January of this year, there was considerable discussion from various stakeholders on whether QM status should provide lenders with a safe harbor or a rebuttable presumption of compliance with their obligation to reasonably determine whether a borrower can afford to repay a mortgage. CRL and other consumer groups supported a QM rule that provided a rebuttable presumption of compliance so all borrowers would have the ability to challenge whether a lender had appropriately fulfilled its Ability to Repay obligations. Lenders generally supported a rule that provided all QM loans with a safe harbor of compliance, meaning that no borrower receiving a QM loan could raise a legal challenge.

The CFPB's final rule establishes a two-tier system where the vast majority of loans will have a safe harbor and others will have a rebuttable presumption, and the threshold between the two depends on the loan's annual percentage rate (APR) relative to the average prime offer rate (APOR). A loan's APR is a figure that represents the overall cost of the loan, including both the interest rate as well as some specified fees. The APOR is a calculation that reflects the APR for a prime mortgage, and these figures are released on a weekly basis.

While this provision gives the vast majority of loans a safe harbor of compliance, the CFPB's rules do allow borrowers to hold lenders accountable on the riskiest types of mortgages. For the general definition using a 43% debt-to-income ratio threshold and the definition based on eligibility for purchase or insurance by Fannie Mae, Freddie Mac and government agencies, the dividing line between a safe harbor and a rebuttable

[36] *Id.*, at 6527.

presumption is 1.5% above APOR for a first-lien mortgage and 3.5% above APOR for a subordinate lien mortgage. Those loans above the thresholds have a rebuttable presumption of compliance whereas those loans below the thresholds have a safe harbor of compliance. The CFPB adjusted these figures upward for loans obtaining QM status under both the definition for small creditors holding loans in portfolio and for the definition for balloon loans, resulting in both first-lien and subordinate lien mortgages having a safe harbor up to 3.5% above APOR.

As stated at the outset, the CPFB's Qualified Mortgage definition has hit the right balance of protecting consumers and facilitating compliance with these rules. The broad definition using clear, bright lines – in addition to providing borrowers in the riskiest mortgages with the opportunity to raise a legal challenge when necessary – will create incentives to avoid future subprime lending abuses and unnecessary foreclosures. At the same time, the four QM standards will also ensure that there is access to responsible credit and that lenders are able to comply with these standards.

Thank you for the opportunity to testify today, and I look forward to answering your questions.

June 18, 2013

Testimony of

James Gardill

On behalf of the

American Bankers Association

before the

Financial Institutions Subcommittee

of the

Financial Services Committee

United States House of Representatives

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Chairman Capito, Ranking Member Meeks, my name is James Gardill, Chairman of the Board of WesBanco. I appreciate the opportunity to be here to represent the American Bankers Association (ABA) to present the views of the ABA regarding the new Ability to Repay and Qualified Mortgage rules. ABA represents banks of all sizes and charters and is the voice for the nation's $14 trillion banking industry and its two million employees.

Before I discuss the impact of the new rules on mortgage markets, let me describe a bit about my bank. We are a $6.1 billion institution in Wheeling, West Virginia. We have 118 offices in West Virginia, Ohio and Pennsylvania. We are active mortgage lenders and currently hold $1.3 billion in outstanding home mortgage loans.

The mortgage market comprises a substantial portion of the GDP in our economy and touches the lives of nearly every American household. The new Ability to Repay (ATR) and Qualified Mortgage (QM) rule represent a fundamental change in the housing-finance market. It is critical that these rules make sense and do not end up hurting creditworthy Americans that want to own a home.

Unfortunately, the Ability to Repay/QM rule, however well intentioned, will end up restricting mortgage credit making it more difficult to serve a diverse and creditworthy population. Under the ATR rule, underwriters must consider a borrower's ability to repay a mortgage loan, despite having no binding guidance on how to determine ability to repay. Qualified Mortgages are designed to offer a "safe harbor" within which loans are assumed to meet the ATR requirement. However, the definition of QM—which covers only a segment of loan products and underwriting standards and serves only a segment of well qualified and relatively easy to document borrowers—could undermine the housing recovery and threaten the redevelopment of a sound mortgage market.

The problem is three-fold: First, the general non-QM segment is very unclear and compliance is uncertain. More pointedly, the heightened penalties and liabilities applicable in the Ability to Repay rule are tremendously burdensome. Given the legal and reputational risks imposed by this regulation, banks are not likely to venture outside the bounds of the QM safe harbors.

Second, the new rules create a narrowly defined box that consumers must fit in to qualify for a QM-covered loan. Since banks will make few, if any, loans that do not meet QM standards, many American families across the country that are creditworthy but do not fit inside the QM "box," will be denied access to credit. In practice, this also likely means that less affluent communities may not be given the support they need to thrive. These rules may leave many communities largely underserved in the mortgage space.

In particular, I am concerned that our bank will be unable to continue a charitable plan we administer designed to promote homeownership among families that would otherwise not be able to own a home. Loans made under our Laughlin plan, which I will discuss in greater detail below, would likely not qualify for QM status, and at least some of the loans made under the plan will not meet ATR requirements, meaning we would not be able to make them at all.

Third, even if banks choose to make loans only inside the QM framework, they will still face a number of risks and uncertainties that create disincentives to lend. Some loans that fit within the QM framework are only partially covered by the protections offered by QM. These loans, specifically higher interest rate loans, still carry both higher credit risk and now, under QM's rebuttable presumption, liability risk, and as a result, banks will be hesitant to offer them. This means that banks will be limited to offering loans to only the best qualified borrowers. The end result of this will be limiting credit to credit-challenged communities or demographics. Thus, in practice, the QM box ironically may conflict with fair lending rules and goals of the Community Reinvestment Act.

The rulemaking has left banks little time to comply with the QM regulations despite the wide-reaching market implications and tremendous amount of work banks must undertake to comply with these rules. Currently, these rules are scheduled to go into effect in January of 2014. Between now and then banks must fully review all of the final rules; implement new systems, processes and forms; train staff; and test these changes for quality assurance before bringing them online. We must get this right, for the sake of our customers, our banks' reputations, and to promote the nascent recovery of the housing market. For some institutions, stopping any mortgage lending is the answer to this unreasonable deadline because the consequences are too great if the implementation is not done correctly.

These rules need to be revised so that they help the economy and at the same time ensure that the largest number of credit worthy borrowers are able to access safe, quality loan products. In order to do this, we need to extend the existing deadlines as well as address outstanding issues to ensure that all creditworthy borrowers have access to credit:

In my statement today, I would like to make three key points,

- The QM rule will limit mortgage lending because the QM guidelines narrow lending parameters and impose high risks on those lending outside of these parameters;
- Even within the QM framework, the ability to lend to a diverse group of consumers may be difficult and may lead to fair lending and Community Reinvestment Act concerns; and
- Because of the wide reaching implications for the mortgage business and credit availability, the implementation date should be delayed to assure that banks have the time to fully comply with the rule's requirements.

I. The QM rule will limit mortgage lending because the QM guidelines narrow lending parameters and impose high risks on those lending outside of these parameters

The Dodd/Frank Act requires that lenders show that a borrower has an ability to repay a loan, which is a practice that all good lenders, and certainly any that intend to remain in business for the long-term have always followed. Unlike many prior federal actions in this area, the new ATR requirement and the QM provisions do not merely impact disclosures or timing. The rules create a fundamentally new paradigm for residential mortgage lending by creating a narrow framework, outside which there are significantly higher risks to lenders.

ABA believes that the Ability to Repay standard in Dodd/Frank has the very commendable goal of driving out bad products and bad lenders from the marketplace. But the ATR/QM rule achieves that goal at a significant cost. It takes away some necessary flexibility for good lenders to make some loans because they simply will not meet Ability to Repay standards. The Consumer Financial Protection Bureau (CFPB) has recognized this, and tried to make accommodations for at least some of the instances where Ability to Repay can stifle good lending. On May 29, 2013 the CFPB exempted certain non-profit lenders serving specific populations from Ability to Repay requirements. This was a step in the right direction, but much more is needed. Take for example a loan made by a community banker to a customer, who may not meet traditional underwriting requirements, but who is known and trusted by the banker from years of personal interaction. Under the Ability to Repay standard, that loan most likely will not be made. The regulatory, litigation and reputational risk will simply be too great. While it is true that loans like that are the exception and not the rule, they do matter, especially to the borrower in need of that type of loan.

In crafting the QM, the CFPB did manage to encompass the majority of loans being made today. A loan that is eligible for sale to Fannie Mae or Freddie Mac is a QM loan. With further refinements recently made by CFPB, many balloon loans made by an institution of $2 billion in assets or less will be considered QM, so long as that institution holds the loan in portfolio and does not make more than 500 mortgage loans per year. But not all loans will be QM loans. A loan exceeding Fannie and Freddie conforming loan limits, even if it meets all other GSE eligibility standards, is not a QM loan. Many loans made by a portfolio lender with more than $2 billion in assets, and otherwise equivalent to a QM loan made by a lender with less than $2 billion in assets, will not be considered a QM loan unless the borrower's debt-to-income ratio is at 43 percent or lower. Similarly, a loan made by a portfolio lender under $2 billion in assets who made 480 mortgage loans in the last year may qualify as a QM loan, but the same loan, made by a lender with $1 billion in assets but who made 502 loans in the last year, would not qualify as a QM loan. As you can see, these are arbitrary standards and their complexity is likely to lead to some very strange outcomes.

The increased risks associated with making loans that fall outside of the QM framework mean that many banks, including mine, will not lend outside of QM and many borrowers will be unable to find lenders willing to make them loans. The QM rule establishes strict guidelines under which mortgage loans are granted protection from certain lawsuits. Banks that choose to lend outside of this framework face significantly increased risks of lawsuits related to ATR requirements. As a result of these increased risks, these loans are much less likely to be made, leaving many potential borrowers without access to credit. In the event that these non-QM loans are made, they will be far costlier, burdening the families least able to bear the expense. The limits on credit availability will be felt keenly by those borrowers who are unable to obtain a loan, but may also be felt by the broader economy. Cutting credit to this market now, just as it is showing signs of a recovery, could prove a sharp blow to an already struggling market. A further delay in the housing recovery would be felt by all Americans, both through the value of their homes and the impact of housing on the broader economy.

Risks Posed to Lenders from ATR and QM

The ATR Requirement prohibits lenders from making a covered residential mortgage loan unless the lender has made a good faith determination that the consumer will have a reasonable ability to pay the loan according to its terms. Lenders must take the following eight factors into consideration when assessing a borrower's ATR:

- Current or reasonably expected income or assets;
- Employment status, if creditor is relying on employment for repayment;
- Monthly payment on covered loan;
- Monthly payment on a simultaneous loan secured by the same property;
- Monthly payment for mortgage-related obligations;
- Current debt obligations, alimony and child support;
- Monthly debt-to-income ratio ("DTI") or residual income;
- Credit history.

Although these eight factors afford much latitude, the concern is that every technical detail of the underwriting decision will have to be documented and demonstrably verified. As a consequence of this ATR Requirement, foreclosing on a delinquent borrower will likely become significantly more difficult because counsel for many delinquent borrowers will attempt to put the lender on trial, by arguing that the borrower is delinquent on the loan because the lender made a loan that it should have known the borrower would not be able to repay. A borrower who is able to mount a strong challenge in this regard effectively may be able to prevent a foreclosure or negotiate more favorable terms on a modified loan. While that is appropriate if in fact a lender did not appropriately consider a borrower's ability to repay, it should not be the outcome if ability to repay was properly determined, but the lender cannot, years later, prove that they met every element of the guidelines. Whether an ATR determination is reasonable and in good faith will depend not only on the creditor's underwriting standards, but on the facts and circumstances of a particular loan and how the creditor's standards were applied to those facts and circumstances. The authorization of the use of oral evidence and post-closing factors in judging such decisions opens lenders to new challenges that cannot be mitigated. This provides a borrower the opportunity to argue that a creditor's underwriting standards were too lax and that the creditor failed to appropriately apply its standards to the specific circumstances of the borrower. It also puts a burden on the lender to demonstrate the appropriateness of its policies and the strength of its controls.

Some specific risks associated with making loans outside of QM are as follows:

Litigation Risk

There are many and varied ways to demonstrate an ability to repay a loan. There are also many and varied ways to challenge a showing of ability to repay. The statute recognizes that, and appropriately did not try to codify all underwriting decisions. But that also means that challenges based on Ability to Repay grounds will be litigated, and there is much uncertainty associated with potential litigation.

The CFPB did not adopt any binding regulations regarding the adequacy of an ATR determination. According to the regulations, the underwriting standards must be "reasonable." Given the rule's abstract guidance, this issue will ultimately be determined in court proceedings relating to individual loans. In those cases, the court will have to determine the nature and extent of discovery that it will permit, and then make individual substantive decisions as to whether the ATR requirement was satisfied in a particular case. Over time, it can be expected that courts will develop standards for both of these issues to which lenders will have to adjust. But in the near term, lenders will face a significant level of uncertainty when they are presented with borrower ATR claims. They are essentially on their own when it comes to implementing the rules and adopting policies and controls. That creates a significant responsibility on banks, their managements and boards of directors.

Statutory Liability for an ATR Requirement Violation

A lender that is found to have not complied with the ATR requirement is subject to general Truth in Lending Act damages and special ATR statutory damages that may be up to the sum of all finance charges and fees paid by the consumer. Furthermore, when a lender or an assignee initiates a foreclosure action, a consumer may assert an ATR violation as a basis for recoupment or setoff. Thus, from a practical perspective, an undeniably delinquent borrower may be able to prevent a foreclosure. Borrower's counsel, in many instances, will use the prospect of an ATR challenge to seek to arrive at a resolution with a creditor that leaves the borrower in possession of the property on new loan terms. In short, in light of the potential for a proven violation, it is possible that the lender may find it more advantageous to actually forgive a significant portion of the remaining indebtedness, thereby raising issues as to the value of a portfolio of loans with the same characteristics.

Safety and Soundness Concerns

A bank is subject to enforcement action if it violates laws or regulations or engages in unsafe and unsound practices. The question therefore arises—will non-QM loans be deemed "safe and sound"? Will such loans carry higher risk weights or be weighed as "inferior" to QM loans? In addition, banks that make non-QM loans may be subject to claims that certain loans do not meet the ATR requirement and, thus, violate the Truth in Lending Act and the CFPB's ATR Rules. These claims may be made by borrowers as well as regulators. Widespread claims of this type could potentially be viewed as constituting an unsafe and unsound practice. Finally, to the extent that banks lend beyond the limits of a QM, any weakness in the portfolio of the bank may be attributed to unsafe and unsound lending practices. These and other issues related to the ATR Rules could form the basis for an enforcement action against a bank.

II. Even within the QM framework, many concerns remain that could limit credit availability to a diverse group of consumers

Even banks making loans exclusively within the QM framework face a number of risks and remaining questions that could limit the availability of credit to a diverse group of consumers. Banks cannot simply eliminate the risk introduced by the ATR requirement by exclusively making QM loans. Some loans made within the QM framework, specifically at higher interest rates, are only partially covered by QM's protections

Potentially, it also means that my bank will face risks associated with NOT lending outside of the QM, including difficulties meeting our Community Reinvestment Act obligations, and potentially even fair housing and fair lending claims based upon "disparate impact" analysis. It is quite the "Catch-22" when a bank attempts to limit its regulatory, litigation and reputational risk by staying within government prescribed rules, only to be subject to possible regulatory, litigation and reputational risks for NOT straying outside those rules.

A bank's compliance with the fair lending laws is an important concern. Since QM loans naturally will create tighter underwriting standards that may narrow the range of qualified borrowers, how a bank approaches compliance with the ATR Rules could have an adverse impact on the bank's ability to respond to a governmental fair lending inquiry, or to a private party claim under the fair lending laws, i.e., the Equal Credit Opportunity Act and the Fair Housing Act.

Limiting loans to QM loans will also have a large impact on the communities we serve, limiting credit to families that may need it the most. If banks are only making loans within the QM structure, many lower-income borrowers may be unable to get the credit they need to purchase a home. At my bank in particular, we have a charitable program, the Laughlin Plan, designed to encourage the heads of large families to own their own homes. This is a charitable program created under the Will of George A. Laughlin, and administered by the bank, which provides financial aid to the heads of families residing in Ohio County, West Virginia. Under the terms of Mr. Laughlin's Will, applicants must be "sober, industrious, and have good general character." This aid is made available only to those who, without the aid of such assistance, would find it difficult, if not impossible, to acquire homes on their own. The Plan provides interest free loans and insurance to these families. The Plan has been in place since 1951 and has helped hundreds of families achieve home ownership in Ohio County, West Virginia. We currently have approximately 100 active loans under this program, providing homes to families who otherwise would not be able to afford one. We are concerned that, under the new rules, loans like these will not qualify for QM status, and as a result it will be very difficult to continue this program that has given so much back to the community. Of even greater concern is the fact that some borrowers served by this program would not meet the Ability to Repay standards and thus could not be helped by this, or any other bank program going forward.

III. Given the complexity of the risks and the new systems associated with QM, implementation deadlines must be extended.

Given the complete reshaping of the relationship between mortgage borrowers and lenders compelled by these new rules, there is much work to be done before banks can be ready to implement them. These ATR/QM rules do not come alone—there are currently 6 rules that are being finalized simultaneously, and these new rules are thousands of pages in length and establish a broad new regulatory framework for mortgage lending and servicing activities. These rules affect the entire mortgage-lending industry, including lenders, service providers, appraisers, escrow agents, and virtually anyone with a relationship to the mortgage lending process. The new rules will significantly reshape the housing-finance market, which comprises a substantial proportion of our country's gross domestic product and touches the lives of nearly every American household. If we do not get this right it will have a negative impact on banks, our customers, and the nascent recovery of the housing market.

Our most urgent concern right now is ensuring we have sufficient time to fully review all of the final rules; implement new systems, processes and forms; train staff and test these changes for quality assurance before bringing them online. Although most of the changes mandated by the new rules call for a 12-month implementation period, the actual amount of time available to financial institutions to comply is in fact much shorter. In order to manage year-end regulatory and tax reporting requirements, many institutions have an information technology "freeze" between November and early January. Because it is not possible to test or revise the new mortgage compliance systems during the lock-down period, the compliance deadline will effectively be November, 2013.

Regulatory implementation is further complicated by the fact that many banks commonly rely on vendors for software updates and system upgrades. Many banks report their vendors are not yet ready to provide the necessary updates to the individual institutions and some vendors may not do so until late summer or early fall.

A vendor recently told its community bank client that it will not have the majority of its updates out until November 22nd. This means that the vendor's customers will have 7 weeks to customize, update, and train – with the Thanksgiving, Christmas, and New Year's holidays sandwiched in between, along with the year-end freezes for purposes of regulatory reporting.

In addition to these challenges, financial institutions face the difficult prospect of implementing the new mortgage rules with important provisions of the Ability to Repay/Qualified Mortgage rule still outstanding and many significant questions yet unanswered. Since the release of the final mortgage rules, ABA and a group of other trade associations have provided the CFPB with detailed requests for guidance on specific provisions of the rules which the industry finds unclear or confusing. These requests are not a complete list, and it is very likely other issues will emerge as financial institutions, and their third-party vendors, progress through their implementation plans. However, clarity on these issues is a necessary prerequisite for our members to fully implement the changes mandated by the new rules.

CFPB has, as recently as May 29th issued additional revisions to the mortgage rules and accompanying staff commentary, and other CFPB proposals are pending. We anticipate these clarifications will provide important information to help our members make strategic decisions regarding their business models and with regulatory implementation. Bankers are very concerned about the prospect of making such decisions while the mortgage rules and commentary are in the process of being revised and each revision issued requires further compliance efforts by our members, their vendors and others, all of which takes additional time.

For the reasons outlined above, we ask Congress to urge the CFPB for quick action on providing the industry with guidance and for more time than the allotted 12-month period to comply with the new mortgage rules. The requirements mandated by the new rules are overwhelming and the short implementation period, along with the lingering uncertainty surrounding the final rules, poses additional compliance challenges. While we welcome the CFPB's recent issuance of the Small Entity Compliance Guide for the Ability to Repay and Qualified Mortgage Rule, as well as recent final clarifying rules on points and fees and balloon loans, these do not obviate the need for a longer implementation period. The industry needs adequate time to review and implement the underlying final mortgage rules and their continuing modifications in order to be in full compliance.

We have suggested in the past, and we repeat this request now, for the CFPB to use its exemption authority to extend implementation of the mortgage rules by 12 months in order to facilitate an orderly compliance process. Without more time to comply, we are concerned certain lenders may choose to mitigate the resulting operational risks by reducing, or even eliminating, their mortgage lending activities in the short-term. This will be devastating to the industry and reduce mortgage loan options for consumers at a time when all agree there should be an increase in responsible mortgage lending. Lacking that action by CFPB, we urge Congress to statutorily extend the implementation date for the mortgage rules by one year, to January of 2015.

Conclusion

Despite the good intentions behind the QM rules, as currently designed, these rules will restrict, rather than facilitate, credit to mortgage borrowers, and most particularly, borrowers on the margins. The ATR and QM rules represent a fundamental change in housing finance. This is an important market, representing a substantial portion of GDP. As such, it is critical that we get these rules right. Although the QM rule provides a necessary "safe harbor," its relatively narrow scope will reduce availability of housing credit. The risks associated with lending outside of QM standards mean few loans will be made outside of the QM designation. The result will be limited credit availability to many households across the country. Even if banks make loans exclusively within the QM framework, they face a number of risks that could discourage them from making loans. Moreover, the short timeline to comply with these rules will leave many banks scrambling to meet the new regulations, and may reduce the credit availability further unless timelines are extended.

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TESTIMONY
OF
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ON BEHALF OF THE
CREDIT UNION NATIONAL ASSOCIATION

BEFORE THE
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT
COMMITTEE ON FINANCIAL SERVICES
UNITED STATES HOUSE OF REPRESENTATIVES

HEARING
ON
"EXAMINING HOW THE DODD-FRANK ACT HAMPERS HOMEOWNERSHIP"
JUNE 18, 2013

Testimony of
Mr. Jerry Reed
Chief Lending Officer
Alaska USA Federal Credit Union
On behalf of the
Credit Union National Association

Before the
Subcommittee on Financial Institutions and Consumer Credit
Committee on Financial Services
United States House of Representatives

Hearing on
"Examining How the Dodd-Frank Act Hampers Homeownership"
June 18, 2013

Chairman Capito, Ranking Member Meeks, Members of the Subcommittee:

Thank you very much for the opportunity to testify at today's hearing. My name is Jerry Reed, and I am the Chief Lending Officer of Alaska USA Federal Credit Union, a federally charted credit union, headquartered in Anchorage, Alaska, serving 471,000 members. I am testifying today on behalf of the Credit Union National Association (CUNA), the largest credit union advocacy organization in the United States, representing America's state and federally chartered credit unions and their 96 million members.

Earlier this year, the Consumer Financial Protection Bureau (the Bureau) issued a final "Ability to Repay" rule to implement provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act regarding the borrower's ability to repay a residential mortgage loan and establishing requirements for a qualified mortgage (QM) under the Truth in Lending Act, which is implemented by Regulation Z. On May 29, 2013, the Bureau finalized additional amendments to the rule.[1] The amended rule extends the qualified mortgage definition to loans made by and held in the portfolio of a credit union that originates 500 or fewer first-lien loans per year and has less than $2 billion in total assets, even if the consumer's debt to income ratio exceeds 43%.

[1] http://files.consumerfinance.gov/f/201305_cfpb_final-rule_atr-concurrent-final-rule.pdf

These amendments made needed changes to the QM rule and were well received by credit unions. At the outset, America's credit unions want to commend the Bureau for listening to the concerns of credit unions, and for incorporating many of our concerns into the new rule. The Bureau has always had an open door policy and encouraged credit unions to voice their concerns, for which CUNA is grateful. Nevertheless, credit unions continue to have serious apprehensions about how the QM rule will be implemented and believe that it could have the unintended effect of reducing credit union members' access to credit.

While we appreciate the fact that the Bureau has provided a modest exemption for small volume originators, we question the need to apply this rule to credit unions in the first place, and urge the Bureau to consider exempting credit unions from the rule entirely. Credit unions were created to promote thrift and provide access to credit for provident purposes to their members. The credit union structure and historical performance of credit union mortgage loan portfolios strongly support a full credit union exemption from the QM rule. As not-for-profit financial cooperatives, credit unions are owned by the members that they serve. This fundamental difference between the for-profit and not-for-profit sector of the financial services industry provides a significantly different incentive structure for those managing the institutions. In addition, credit unions are primarily portfolio lenders, typically selling less than a third of their new originations. The fact that most of the loans they make will be held in their own portfolios is further incentive for them to be particularly attentive to the applicant's potential ability to repay.

The value of this difference is clearly seen in the credit unions' historical mortgage lending performance. Prior to the Great Recession, annual net charge-off rates on residential mortgage loans at both banks and credit unions were negligible, less than 0.1%. However, as the recession took hold, losses mounted. At credit unions, the highest annual loss rate on residential mortgages was 0.4%. At commercial banks, the similarly calculated loss rate exceeded 1% of loans for three years, reaching as high as 1.58% in 2009.[2]

Simply put: credit unions have every incentive to evaluate a member's ability to repay because their members are also the owners. It is not in the interests of a credit union or its other

[2] Based on FDIC and NCUA data.

members to lend money to a member likely to default. As a result, credit unions employ strong underwriting standards, consistent with the spirit of the QM rule. Credit unions also have a history of tailoring lending products to meet the needs and demands of their members. Credit unions have proven they can provide credit on fair terms to borrowers who cannot meet QM standards, but are good credit risks nevertheless. Congress and the regulators should encourage financial institutions to offer loan products focused more on the individual. Unfortunately, depending upon how the QM rule is interpreted by the prudential regulators and how it is utilized within the marketplace, the QM rule may stop this from happening. The unfortunate result will be that some members who would otherwise have qualified for a mortgage from their credit union may not receive loans.

Credit unions worry that the QM rule will make it all but impossible for credit unions to write non-QM loans because the standard, designed to be an instrument of consumer protection, may serve as an instrument of prudential regulation, effectively setting a bureaucratic standard for loan quality. Further, we have concerns that there may not be a viable secondary market into which credit unions can sell non-QM loans. If the prudential regulator will not permit credit unions to hold non-QM loans and the secondary market will not accept them, credit unions will not be able to write them. To the extent that happens, credit unions will not be able to meet the mortgage lending needs of a sizeable segment of their membership. In addition to these concerns, we also have specific views and concerns regarding the 43% debt-to-income ratio requirement, the 3% limitation on points and fees, the definition of rural and underserved area, and the bifurcated approach to the QM rule.

An Instrument of Consumer Protection Becomes an Instrument of Prudential Regulation

As this rule is implemented, it is important that Congress and the Bureau work closely with prudential regulators to ensure that this instrument of consumer protection does not become an instrument of prudential regulation. We have significant concerns that the National Credit Union Administration (NCUA) examiners will want to severely restrict the ability of credit unions to keep non-QM loans in their portfolio after the rule goes into effect. The possibility exists that NCUA examiners will determine that mortgages that do not enjoy the benefit of the qualified mortgage rule's safe harbor are a safety and soundness concern. Examiners may also be critical of credit unions and assess their CAMEL ratings accordingly if credit unions make mortgages that do not meet the QM standards.

The potential for negative supervisory actions are a real concern for credit unions, and will contribute to the decline or elimination of non-QM lending unless Congress and the Bureau send a strong message to examiners.

Bureau Director Richard Cordray has noted the importance for the continued availability of non-QM loans. Recently, he told a gathering at the National Association of Realtors:

> Qualified Mortgages cover the vast majority of loans made in today's market, but they are by no means all of the mortgage market. This point is quite important, and it should not be misunderstood. Those lenders that have long upheld strong underwriting standards have little to fear from the Ability-to-Repay rule. These lenders, including many of our community banks and credit unions, have seen the strong performance of their loans over time. Nothing about their traditional lending model has changed, and they should continue to offer such mortgages to borrowers whom they evaluate as posing reasonable credit risk – whether or not they meet the criteria to be classified as Qualified Mortgages. We all benefit by recognizing and sustaining responsible lending wherever we find it in the mortgage market.[3]

It is important that other regulators follow the lead of the Bureau on this matter. Non-QM loans and the availability of credit to worthy-borrowers should be encouraged and not viewed negatively by examiners.

Recent FHFA Action Raises Concern That a Viable Market May Not Exist for Non-QM Loans

Traditionally credit unions have been portfolio lenders, meaning they hold mortgages they make on their books. However, in recent years, this trend has begun to change as credit unions have sold more mortgages to Fannie Mae, Freddie Mac and other secondary market participants in order to diversify their portfolio and manage interest rate risk, consistent with directives from examiners. In many cases, credit unions retain the servicing rights on loans they sell into the secondary market.

[3] http://www.consumerfinance.gov/speeches/director-richard-cordray-at-the-national-association-of-realtors/

Selling mortgages into the secondary market allows credit unions to unlock much needed funds in-order to make more mortgages. It also serves an important function of mitigating interest rate risk. When interest rates are low, it is risky for a credit union to hold too many 30-year mortgages in portfolio. We believe credit unions should retain the flexibility they currently have to either hold a loan in portfolio or sell it on the secondary mortgage market based on the needs of the credit union to manage its assets and obligations. While nothing in the rule would prohibit credit unions from selling non-QM loans into the secondary market, if there is a viable secondary market for these loans, we have concerns that the market for these loans may not exist.

In May, the Federal Housing Finance Agency (FHFA) directed Fannie Mae and Freddie Mac not to purchase certain non-qualified mortgage loans after the effective date of the rule.[4] Fannie Mae and Freddie Mac will continue to purchase loans that meet the underwriting requirements stated in their respective selling guides, including loans with debt-to-income ratios above 43 percent; however, other loans issued with terms that are outside the Bureau's QM definition, such as 40-year term loans, or loans with points and fees exceeding the thresholds established by the rule, will not be purchased by Fannie Mae or Freddie Mac. This decision by FHFA may at the very least send a negative signal that creativity in the secondary market is not welcome, thus limiting the ability of credit unions to meet the variable needs of their credit worthy members. We ask the Subcommittee to ensure into the future that Fannie Mae and Freddie Mac will purchase loans originated by a credit union even if they do not meet the QM definition if they otherwise meet GSE standards.

The ability of credit unions to customize their products to meet the needs of their individual members is important because credit unions understand that every member is different; therefore, creating a loan product that fits the needs of the individual or circumstance will, at times, fall outside of the QM boundaries. One need only to look to the origin of credit unions in order to have a better understanding of why being forced to follow the QM rule encounters resistance. Credit unions were created by citizens of similar backgrounds with the mission to extend credit to their member-owners and always look to exhaust every option in order to satisfy a member's needs. This is what makes the credit union experience different.

[4] http://www.fhfa.gov/webfiles/25163/QMFINALrelease050613.pdf

Nevertheless, the FHFA decision leaves the impression that this kind of individualization should be abandoned. As credit unions evolve with the financial markets and member needs, FHFA has essentially thrown a monkey wrench into credit unions' ability to serve their members, adversely affecting consumer's ability to access credit.

The Bureau Should Expand the Small Loan Originator Exemption to Treat All Credit Union Loans as QM Loans

In addition to ensuring that regulators do not treat loans that do not meet QM standards as unsafe loans and ensuring that the FHFA permits Fannie Mae and Freddie Mac to purchase loans that do not meet QM standards, Congress should encourage the Bureau to treat all mortgage loans made by credit unions as QM loans, as we have urged to the agency.

Ability to repay is one of many factors that determine a loan's performance, but it is a critical factor because, without it, the loan certainly will not perform. The Bureau recognized this when it cited a November 2012 Federal Reserve Board report entitled, "Charge-Off and Delinquency Rates on Loans and Leases at Commercial Banks," to make the point that "mortgage loan delinquency and charge-off rates are significantly lower at smaller banks than larger ones."[5] However, we were disappointed that the Bureau did not take into consideration the differences in delinquency and charge-off rates between banks and credit unions when considering which classes of transactions and institutions to exempt from the QM rule.

As most have acknowledged, credit unions did not create or exacerbate the financial crisis; rather, credit unions continued to extend mortgage credit to their members throughout the crisis, while many other lenders retracted their lending. As the financial crisis took hold and secondary markets dried up, credit unions increased their first mortgage originations from $54 billion in 2006 to $60 billion in 2007, $70 billion in 2008 and $95 billion in 2009. Despite this strong lending in a very turbulent economy, credit union net charge-off rates for mortgages remained very low.

[5] Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act, Regulation Z, 12 CFR Prt 1026, Docket No. CFPB-2013-0002, RIN 3170-AA34. Page 28.

Credit unions have proven they can appropriately mitigate risk even while tailoring certain loan products to meet members' needs. Appendix I describes first mortgage loan charge off rates at credit unions and banks over the last seven years. As shown in the chart, credit unions of all sizes have remarkably low net charge-off rates, and bank losses have been more than double those of credit unions. In fact, aggregate credit union mortgage losses **have never** gone above 0.45%. What this demonstrates is that credit unions across the board are already making mortgage loans that their members have the ability to repay – without having to be directed to do so by the federal government – and they should not be subjected to additional regulatory burden that would hinder their ability to meet their members' needs or reduce their members' responsible access to credit. Credit union mortgage loans are not the loans with which the Bureau or others should be concerned. If anything, our regulators and Congress should applaud not-for-profit, member-owned credit unions for their conservative lending practices before, during and after the financial crisis.

As the economy recovers, the credit union model continues to serve credit union members well, but the QM rule has the potential to fundamentally alter that relationship. In fact, had this rule been in effect during the crisis, it is very likely that as the crisis worsened, NCUA examiners would have increasingly frowned on non-QM loans, making it that much more difficult for credit unions to continue to lend when other providers did not.

We believe it is reasonable for this Subcommittee to urge the Bureau to reconsider why credit unions, in light of the strong performance of their mortgage loans, should be subject to this rule in the first place. All loans originated by a credit union, regardless of its asset size, should enjoy qualified mortgage status.

Other Issues

Debt-to-income Ratio

In order for a loan to be considered a "qualified mortgage" the consumer's total monthly debt to total monthly income at the time the loan is made cannot be higher than 43%. The Bureau has taken steps to provide clarity in this area and Director Cordray has indicated his support of non-qualified mortgage loans. However, there is a concern about the way in which non-qualified mortgage loans will be treated by prudential regulators. Credit unions often write mortgage loans for members that have a 45% debt-to-income ratio and may even go as high as a 50% debt-to-income ratio under certain limited circumstances. Even so, our mortgage losses remain very low.

The Bureau acknowledges that a higher debt-to-income ratio is warranted in some instances and the amended QM rule provides assurances that lenders with less than $2 billion in assets and make 500 or fewer first-lien mortgages per year have the ability to serve a credit worthy borrower. The rule would allow a consumer's debt-to-income ratio to exceed 43% in these limited instances. In short, exempting institutions of $2 billion in assets that originate 500 or fewer first-lien mortgages is not meaningful for the credit union system. Credit unions have proven their worth to the mortgage market in their high performance rates of their first-lien mortgage products. Accordingly, all first-lien mortgages originated by a credit union should enjoy qualified mortgage status.

Points and Fees

For a mortgage to be considered a "qualified mortgage," total points and fees generally may not exceed 3% on a loan of $100,000 or greater. These fees include affiliate and non-affiliate charges such as title insurance, surveys, appraisal fees, underwriting, processing and application fees. While these amounts are indexed for inflation, these limitations may be problematic for some credit unions. As the loan amount decreases, certain fees cannot decrease as some fees are fixed and not dependent upon the size of the loan. The smaller the loan amount, the easier it is for fees to constitute a higher percentage of the total loan. This is especially true as the fees are currently defined as including loan originator compensation, and affiliate fees. Many credit unions work with affiliated title companies, for example, to provide the lowest costs for members on title insurance products. However, since affiliated title company fees under the current rule would be included in the points and fees calculation, it may appear to a consumer that an estimate from a non-affiliated title insurance provider is less expensive than the title insurance under the credit union's affiliate arrangement, which is in fact not the case.

The revised rule the Bureau issued does provide some relief to small financial institutions in regard to this points and fees concern, but we do not believe the rule goes far enough. If the Bureau wants to provide borrowers with an easy way to compare a mortgage loan APR between providers in their market then this proposed change will not accomplish that objective. It will mislead borrowers by not being able to compare APR rates between affiliated and non-affiliated companies, put affiliated title companies at a competitive disadvantage, and potentially cause borrowers to incur higher closing costs.

Rural and Underserved Areas

While CUNA is disappointed that the Bureau has not already adjusted its definition of rural and underserved areas, we are encouraged that they are still examining "definitions to determine among other things whether these definitions accurately identify communities in which there are limitations on access to credit and whether it is possible to develop definitions that are more accurate or more precise."[6] The Bureau may consider making changes based on the results of this inquiry. We encourage the Bureau to consult with our prudential regulators with regard to their definitions of these terms. The concern CUNA has with the definition in the current rule is that many credit unions make loans to those in rural and underserved communities but the credit union itself may not be based in those communities. Also, underserved individuals may live in areas that would not meet the CFPB's definition of a "rural" or an "underserved" area. If the definition of rural and underserved does not change, these institutions will be limited in the types of products they can offer their members in these areas.

Bifurcated Approach

QM's that are not "higher-priced" receive the full safe harbor, meaning that they are conclusively presumed to comply with the ability to repay requirements. QM's that are "higher-priced" have a rebuttable presumption that they comply with the ability to repay requirements, but consumers can rebut that presumption.

Under the rebuttable presumption, a court could find that a mortgage originated by a creditor originated as a higher-priced QM, and the consumer can argue that the creditor violated the Ability to Repay rule. To prevail on that argument, the consumer must show that based on the information available to the creditor at the time the mortgage was made, the consumer did not have enough residual income left to meet living expenses after paying their mortgage and other debts.

[6] Ibid, 220-221.

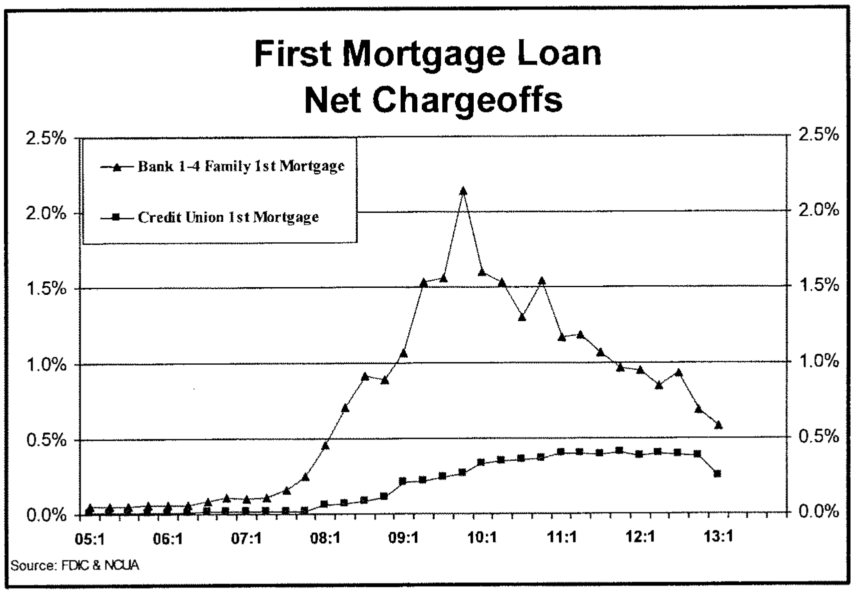
A QM is higher-priced if it is a first lien loan, where, at the time the interest rate on the loan was set, the APR was 1.5% or more over the Average Prime Offer Rate (published weekly by FHLMC), or if it is a subordinate lien loan with an APR that exceeds the APOR by 3.5% or more, using the same test of when the interest rate was set on the loan.

As part of the recently finalized amendments to the Ability to Repay rule, the Bureau has raised the threshold defining which QM loans receive a full safe harbor for loans that are made by small creditors under both a balloon loan and the small creditor categories of QM. The new threshold is now 3.5% (as opposed to 1.5%) for first-lien loans, which is a significant improvement, but only for those that meet the definition of "small creditor," which is under $2B in assets and makes 500 or fewer first-lien loans each year. The balloon loan category requires institutions to meet the definition of "small creditor" and provides that these lenders can make balloon loans for a two-year transition period, even if they are not located in a "rural" or "underserved" area as defined by the Bureau. (The original QM rule provided that only creditors operating predominantly in rural or underserved areas would be eligible for the balloon loan QM exemption).

Conclusion

In conclusion, America's credit unions appreciate the improvements that the Bureau has made to the QM rule; nevertheless, we continue to have significant concerns with respect to how other regulators will use the Bureau's regulation to impact credit union mortgage lending, and we question whether the rule should apply to credit unions in the first place. The Bureau has made great improvements but in other areas the Bureau has not done enough to address credit unions' concerns that being subjected to the rule will actually reduce credit availability. We are hopeful that when the Bureau completes its review of the rural and underserved definition, the changes it makes will reflect our concerns. We urge the Subcommittee to address these issues with the Bureau, NCUA, and FHFA. We further ask this Subcommittee to scrutinize the work of the Bureau and urge them to recognize, under the full extent of the law, the characteristics of credit unions and reflect those in the rulemaking process and, where appropriate, exempt credit unions from their rules. Thank you very much for the opportunity to testify at this hearing.

Appendix I



First Mortgage Loan
Net Chargeoffs
Bank 1-4 Family 1st Mortgage
Credit Union 1st Mortgage
2.5%
2.0%
1.5%
1.0%
0.5%
0.0%
05:1
06:1
07:1
08:1
09:1
10:1
11:1
12:1
13:1
Source: FDIC & NCUA

MORTGAGE BANKERS ASSOCIATION
Investing in communities

Statement of Debra Still

On behalf of the Mortgage Bankers Association

House Financial Services Committee Subcommittee on Financial Institutions and Consumer Credit

"Examining How the Dodd-Frank Act Hampers Homeownership"

June 18, 2013

Chairwoman Capito, Ranking Member Meeks and members of the subcommittee, my name is Debra W. Still and I currently serve as President and Chief Executive Officer of Pulte Financial Services, which includes Pulte Mortgage LLC, PGP Title and PCIC Insurance and employs 750 individuals throughout the United States. I am also President and CEO of Pulte Mortgage, a nationwide lender headquartered in Englewood, Colorado, which has helped more than 400,000 homebuyers finance their new home purchases since 1972. Pulte Financial Services is a part of PulteGroup, America's largest homebuilder with operations in 30 states and the District of Columbia.

I appreciate the opportunity to testify again before this subcommittee, this time in my capacity as Chairman of the Mortgage Bankers Association[1] and as a Certified Mortgage Banker (CMB). MBA uniquely represents mortgage lenders of all sizes from the largest federally-chartered institutions to the smallest community lenders who serve the mortgage financing needs of families and neighborhoods throughout the nation.

Background

Your decision to hold a hearing on the residential mortgage lending standards in Dodd-Frank could not be more timely. During the last several months the Bureau of Consumer Financial Protection (CFPB or Bureau) issued the Ability to Repay and Qualified Mortgage Rule (QM) that will profoundly affect mortgage borrowers and those who hope to one day be able to buy a home. The industry is now fully vested in understanding and implementing this rule, building new policies and procedures, re-engineering loan processes, reprogramming mortgage origination systems, and training our personnel before the rule takes effect in January 2014.

In reviewing the Ability to Repay Rule, context is important. Over the past several years, lenders serving homebuyers in America have experienced high levels of uncertainty in the housing markets and in the regulatory landscape.

The good news is we are making progress. By almost any measure, housing is making a recovery. Home starts are up. Home sales are up. Sales prices are increasing in many areas across the country and home affordability remains at historic highs.

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[1] [1]The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

While housing is improving generally, research shows that the higher end of the market is fueling growth while the lower end of the market is actually shrinking. Access to credit is clearly constrained with first-time and low-to-moderate-income borrowers unable to qualify for a mortgage.

As anticipated, 2013 marks the final publication of many key Dodd-Frank rules. MBA applauds the CFPB for getting a great deal right and for their deliberative and inclusive approach.

Having the rules in place has eased uncertainty to some degree but concerns persist that certain aspects of the rules — particularly the Ability to Repay rule — will further tighten credit to otherwise qualified consumers. The 3500 pages of new rules introduce new levels of complexity that could force lenders to be even more cautious than they are today. We are experiencing a marked shift in real estate finance – a shift from regulatory uncertainty to regulatory complexity. Given this prospect, we should all be concerned about the cumulative effect of the new rules on the availability of credit to qualified consumers.

To avoid or at least lessen this possibility, there is considerable work to be done.

First, we need to work collaboratively with both the CFPB and Congress to make sure that the new rules are "right" and that they support access to credit.

Second we must also make certain these rules are aligned with each other and with other regulations so that the totality of the rules fosters rather than frustrates the availability of sustainable credit to all qualified borrowers.

Third, and of upmost importance, the industry needs clear guidance from the CFPB and adequate time to implement the rule.

The Ability to Repay Rule and QM

MBA has consistently supported reasonable ability to repay requirements that will prevent a reemergence of the competitive excesses of the housing bubble.

Even though the mortgage industry has implemented some of the most conservative underwriting standards in decades and riskier mortgage products are no longer available, we appreciate the value of embedding sound product and underwriting standards into law to assure consumers are protected going forward. Establishing an ability to repay requirement, along with an unambiguous set of standards in the form of a clear safe harbor, is a reasonable way to accomplish this.

Nevertheless, as this process moves forward, we must be mindful of the fact that these new rules are arriving amidst some of the tightest credit standards in decades. It is crucial that these rules do not unnecessarily exacerbate the situation.

Dodd-Frank requires that a lender may not make a residential mortgage loan unless the lender 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.

The law provides steep liability, stiff remedies and severe financial penalties for violations. For example, a mortgage lender who fails to comply with the ability to repay requirement for a hypothetical $200,000 loan would face liability on the order of:

(1) Statutory damages of up to $4,000;

(2) All loan fees and up to three years of finance charges paid by the consumer, which on an average loan of $200,000 at 4.5 percent may be approximately $25,000;

(3) Actual damages, which could include, for example, the borrower's down payment (e.g., $20,000 if the down payment was 10%); and

(4) Court costs and reasonable attorney fees associated with the claim, which could be anywhere between $26,000 and $155,000 (depending on how protracted the court proceedings are).

Dodd-Frank also extends the statute of limitations for a claim based on a violation of the ability to repay requirement from one year to three years. The law also allows a consumer to assert a violation as a claim in foreclosure whenever it occurs, even if the claim arises far beyond three years. The claim may be made against any creditor, assignee or holder of the mortgage as well. This "defense to foreclosure" provision is a major factor in driving investors' and lenders' extreme caution on credit standards.

Against the backdrop of this potential liability and with an eye towards how unpredictable litigation can be, Dodd-Frank provided a principled avenue for compliance. Lenders who make QM loans, which under the law cannot have risky features, must be well underwritten and meet other restrictions (including limits on points and fees), will have assurances that their loans meet the ability to repay requirements.

For this reason, great attention was focused on how QM would be defined.

The Rule Must Support Access to Credit

MBA's Overall View of the QM Rule

As I articulated in my testimony last year, MBA arrived at four principles that we believed should guide the completion of the QM:

- First, the QM needs to be broadly defined in order to reach as many borrowers as possible with safe, affordable and sustainable financing.

- Second, the rule must include clear, specific and objective standards, by incorporating unambiguous requirements.

- Third, the QM should provide lenders and borrowers the legal certainty that meeting the standards will provide them a clearly defined safe harbor so that claims against a loan are limited to examining whether or not the loan is a QM.

- Finally, given the QM's massive effect on the existing market, the rule should be designed in a way that avoids unintended consequences.

We appreciate the efforts of the Bureau that, to a large extent, addressed these concerns.

The rule is relatively broadly defined and temporarily offers the choice of either a 43 debt-to-income ratio or eligibility for GSE purchase or agency insurance or guarantee eligibility. Either pathway to QM qualification remains subject to the rigorous requirements and product feature restrictions embodied in Dodd-Frank and the QM rule.

As I pointed out last year, because of the very significant liability under Dodd-Frank, it is not clear whether and to what extent there will be any substantive non-QM lending particularly lending at affordable prices for creditworthy middle-class families. Some believe non-QM loans will be made but only to the most qualified, wealthiest borrowers and kept in institutions' portfolios. Others believe there will be non-QM lending with significant pricing premiums that will raise costs to borrowers, particularly those least able to afford them. Neither of these outcomes alleviate the need for a broadly defined QM that serves as many creditworthy borrowers as possible.

The rule also offers a legal safe harbor for what the Bureau regards as prime QM loans — those with an APR that is less than 150 basis points over a benchmark rate known as the Average Prime Offer Rate (APOR). Loans with an APR that is 150 or more basis points greater than the benchmark rate are given a less conclusive rebuttable presumption of compliance.

The difference between the safe harbor and rebuttable presumption standards is critically important. A safe harbor simply means that if a lender complies with the exact standards embedded in the rule compliance will be presumed and any litigation will be confined to whether or not the loan is in fact a QM. A safe harbor is not in any way a "pass" from liability for lenders, nor does it deprive consumers of an opportunity for court review. Under either a safe harbor or a rebuttable presumption of compliance, a borrower can seek judicial review of an alleged violation, but in the former instance the review is focused on whether the rule's standards were met.

Under a rebuttable presumption of compliance, however, the scope of the inquiry is potentially far more wide-ranging, with significant variations from one court to another on how the presumption is applied, including when and how extrinsic evidence may be considered beyond the standards. Such an inquiry is more open-ended, unpredictable and far more costly to defend.

Although we appreciate that the Bureau ultimately chose to establish a safe harbor for most of the market, we think it would be beneficial for the CFPB to establish a safe harbor for all loans that meet QM standards.

Given that the CFPB has chosen to bifurcate the QM protections, we believe that the safe harbor should be broadened to cover a larger share of the high quality, well underwritten QM loans that are being made today. In addition, with respect to the rebuttable presumption standard, the CFPB should provide clearer guidance regarding how consumers can rebut the presumption of compliance based on a lack of residual income or how lenders can defend a loan based on a sufficient payment history. Further explanation would facilitate the availability of credit to qualified borrowers whose QM loans do not meet safe harbor standards.

Facilitating Credit to Creditworthy Low and Moderate Income Borrowers

Dodd-Frank limits the points and fees that can be charged to borrowers for a QM loan. The statute specifies 3 percent of the loan amount as the limit but permits adjustments for smaller loans.

Under the final rule in addition to what is traditionally included in points and fees, the definition of points and fees also includes:

(i) charges to lender affiliated (but not unaffiliated) title companies,
(ii) compensation paid to loan originator companies, such as mortgage brokerages,
(iii) amounts for insurance held in escrow and
(iv) loan level price adjustments in the form of additional closing costs.

MBA believes this definition is overly inclusive and will create competitive disadvantages for various business models, reducing choice and ultimately harming consumers. The effects of the overly inclusive points and fees definition will be particularly severe for low-balance loans to low and moderate income borrowers.

Smaller Loans

Under Dodd-Frank, the CFPB has broad discretion to adjust the points and fees limit so that lenders making smaller loans do not exceed the points and fees trigger. The smaller a loan balance, the more difficult it is to meet the 3 percent limit on points and fees.

The QM rule defines a smaller loan as a loan under $100,000 and only permits an increase in the points and fees limit for loans below that amount. However, the average loan size currently is $220,000.

Consider a $150,000 loan, which is typical in many markets in the country. Applying a 3 percent limit to such a loan, only $4,500 would be available to cover fees reflecting the costs of the lender, compensation to a mortgage brokerage, some escrowed amounts and all third party fees of affiliates including title insurance and title services.

Based on this example, many loans are likely to exceed the 3 percent limit and fail to qualify as QMs (even though they meet all other QM requirements). Perversely, the cap on points and fees and the threshold for smaller loans may result in QMs being unavailable to many low and moderate income borrowers, a result we believe is contrary to the statute's purpose.

We believe there are good alternatives to solve this problem, including:

- Removing affiliated title fees, compensation to mortgage brokers and escrow amounts from the points and fees calculation by passing H.R. 1077, the Consumer Mortgage Choice Act; or

- Increasing the dollar amount defining small loans.

Fees of Affiliates

The rule includes in the points and fees calculation charges paid to an affiliate of the lender, including title charges, but excludes charges paid to an unaffiliated company. The rationale behind this decision is not clear and we believe it will end up raising prices and undermining consumer choice.

Some lenders choose to affiliate with title and other service providers to ensure that services are efficient, charges are as estimated and the consumer experience from loan application to closing is seamless, predictable and positive for the consumer. National consumer surveys demonstrate that consumers who take advantage of the one-stop shopping that affiliated businesses report a satisfactory home purchase experience.

Title and title related services are the largest third party settlement cost. Affiliated providers offer services that are competitive in cost with those of unaffiliated providers. The fact that affiliated providers attract business from non-affiliated lenders supports this fact. As might be expected, studies have shown that when affiliates have been excluded from the market, title insurance charges have risen.

In all cases, consumers are free to choose not to use affiliated providers. The Real Estate Settlement Procedures Act (RESPA) requires a clear disclosure of affiliated relationships and their cost and does not permit a consumer to be required to use an affiliated entity. There are clear penalties for forcing a consumer to use a particular affiliate or providing improper inducements to persuade a consumer to do so.

Concerns that lenders may augment their fees through the charges of affiliated companies are not valid. Title insurance premiums, and in many cases fees for title services, are regulated. Forty-four states and the District of Columbia require that title premiums be set by the state, approved by the state, or filed with the state (23 states also include title examinations and searches).

In short, there is no reason for Congress to deny consumers the ability to use affiliated service providers or make it more expensive to do so.

Compensation to Loan Originators from Creditors

We appreciate that with the issuance of its most recent revisions to the QM, the Bureau has modified the rule to exclude from points and fees compensation paid by a lender to its individual employee loan originators. Nevertheless, MBA continues to object to the rule's inclusion of compensation paid by lenders to entities such as community banks, credit unions, local independent businesses and others that broker mortgage loans.

Consumers today obtain the financing they need from lenders with a range of business models. Some consumers use creditors who employ and compensate their own loan officer originators. Others use entities acting as mortgage brokers who may be compensated by wholesale lenders for their origination services. A combination of business models and varying market conditions determine whether consumers may pay some of these costs through direct fees or through their interest rates.

Paying loan originators to steer a borrower into a higher rate or otherwise unfavorable loan has been prohibited under a Federal Reserve rule the CFPB now enforces. The risk of steering consumers to higher cost loans also has been eliminated through these rules, CFPB enforcement powers and the significant new liability provisions. Finally, competition ensures that the costs of loans to consumers through both the retail and wholesale channel are essentially the same.

Under the QM, if two consumers get the same loan, one from a broker and the other from a retail lender, the brokered loan could exceed the points and fees trigger, while the retail loan would be treated as a QM. This perverse result means that the consumer would lose the ability to choose between two loans, from different businesses, that are essentially identically priced.

Notably, for many moderate income borrowers – particularly those with smaller loans or in areas where credit has been scarce such as in rural and certain urban areas – entities offering brokered loans have proven to be the best sources of needed credit. The CFPB's continued discrimination against commissions to entities that broker loans will make these services far less feasible, depriving many consumers of the ability to obtain mortgage financing.

We believe Dodd-Frank was intended to ensure consumers receive sustainable loans, not to pick winners and losers among business models and, as a result, deprive consumers of credit.

Escrow Amounts

Dodd-Frank is ambiguous regarding whether amounts paid to lenders at closing and deposited into an escrow account for the payment of insurance and taxes also are included in the points and fees calculation.

We urge the CFPB to make clear that amounts held for escrow are excluded from the 3 point QM cap.

There is no sound public policy rationale for these fees to be included. Amounts for insurance and taxes are not retained by the lender or its affiliates; they are paid to insurance companies and governmental entities. Additionally, under RESPA, amounts held in escrow that exceed specified limits are returned to the consumer.

A Solution: H.R. 1077, the Consumer Mortgage Choice Act

MBA has repeatedly urged the Bureau to amend the definition of points and fees to exclude affiliated title fees and clarify that loan originator compensation from lenders to brokerages and escrowed amounts be excluded from the calculation for purposes of applying the 3 percent limit.

Despite our belief that the CFPB can make these revisions under existing law, we strongly urge Congress to pass H.R. 1077, the Consumer Mortgage Choice Act. This bipartisan legislation was introduced by Representatives Bill Huizenga, David Scott, Ed Royce, and William Lacy Clay, and cosponsored by over 40 members of the U.S. House of Representatives. The bill addresses each of these items by clearly excluding them from the 3 point QM cap.

Raising the Smaller Loan Threshold

The QM rule provides that loans will be subject to a higher points and fees cap only if the loan amount is less than $100,000. The $100,000 cutoff is insufficient and will deny affordable mortgage credit to families who take out lower balance loans. Smaller loans are particularly a feature of rural and underserved communities.

Under the CFPB's final rule, a covered transaction is not a qualified mortgage unless the transaction's total points and fees do not exceed:

> (A) For a loan amount greater than or equal to $100,000 (indexed for inflation): 3 percent of the total loan amount;

(B) For a loan amount greater than or equal to $60,000 (indexed for inflation) but less than $100,000 (indexed for inflation): $3,000 (indexed for inflation);
(C) For a loan amount greater than or equal to $20,000 (indexed for inflation) but less than $60,000 (indexed for inflation): 5 percent of the total loan amount;
(D) For a loan amount greater than or equal to $12,500 (indexed for inflation) but less 20 than $20,000 (indexed for inflation): $1,000 (indexed for inflation);
(E) For a loan amount less than $12,500 (indexed for inflation): 8 percent of the total loan amount.

These amounts are to be adjusted annually on January 1 by the annual percentage change in the Consumer Price Index.

There is broad discretion under Dodd-Frank for the CFPB to adjust the 3 percent limit on points and fees further, and MBA has recommended such an adjustment to the Bureau. However, at this writing, it does not appear the CFPB is prepared to address concerns about small loan access. Consequently, MBA would support modification of H.R. 1077 to increase the small loan threshold to $200,000 and increase the points and fees limit for loans falling under it to 4 percent. This approach would solve the problem of smaller loans becoming unavailable or more costly to low and moderate income families.

Right Sizing the APR/APOR Definitions to Extend QM Credit to Creditworthy Borrowers

MBA believes that most lenders and mortgage investors, at least for the immediate future, will confine themselves to QM safe harbor loans. Importantly, these loans will come with the most favorable, affordable rates. QM rebuttable presumption loans will be more challenging and costlier simply because the risks are greater.

Under the rule, only mortgages where the APR is less than the 150 basis points over the benchmark APOR qualify for the QM safe harbor. Having analyzed the methodology underlying the determination of the APOR and the components of the points and fees test, an increase in the spread to 200-250 basis points for all loans is warranted.

The APOR is calculated based on the Freddie Mac Primary Mortgage Market Survey (PMMS). In recent quarters, the PMMS has fallen well below MBA survey rates, at times by as much as 20 basis points. At least two-thirds and possibly as much as 80 percent of the rate quotes that are included in the PMMS are for purchase loans. However, purchase loans are typically quoted at lower mortgage rates than those for refinances, with the spread between the two ranging up to 25 basis points for some lenders. This causes the PMMS to be systematically biased against refinance mortgages. This bias is particularly troublesome in markets like today's, where approximately 70 percent of mortgage applications and a similar percentage of mortgage originations are for refinance loans.

In today's market, if refinance loan rates are benchmarked against an APOR based on the Freddie Mac PMMS as in the CFPB's rule, it can be anticipated that a large number of these refinance loans could exceed the QM's 150 basis points limit for the safe harbor even if they met exactly the same standards as purchase loans that fell within the spread and were being offered at prevailing rates.

There are also issues with the applicability of a particular APR-APOR comparison to some of the loan products currently being offered. APORs are calculated taking into consideration whether the rate is fixed or adjustable, lien status, and the length of the loan term. There is a significant weakness in the comparability of APORs for ARM loans because they are not necessarily calculated the same way. For instance, if the APR is calculated using an initial rate that is higher than the fully-indexed rate, the APOR should be calculated the same way. Also, if the APR is calculated using the greater of the initial rate or the fully-indexed rate using the maximum margin the APOR should be calculated the same way.

Finally, there is an additional methodological problem with the PMMS around 20-year loans. These loans are compared to survey rates for 15-year loans, which tend to have significantly lower rates. Twenty year maturities tend to track 30-year rates more closely, leading to the result that many common 20-year loans could exceed the 150 basis points over APOR safe harbor definition simply due to a fault with the underlying APOR calculation, not any feature or aspect of the loan.

While these issues are significant, PMMS still provides a unique data set stretching back decades that could be compromised by methodological changes today. As I have testified, however, we believe lenders will be extremely wary of originating loans that fall outside of the safe harbor for the foreseeable future following the rule's implementation. For these reasons, rather than completely reworking the PMMS or seeking to establish a new survey, MBA believes the CFPB should resolve these issues by adjusting the spread which defines safe harbor and rebuttable presumption QMs.

Accordingly, the safe harbor for all loans should extend to APRs that are 200-250 basis points over their comparable APOR. This is a better solution than introducing a variety of disparate calculations for different products that will increase regulatory burden and confusion. The CFPB itself has repeatedly noted the safe harbor does not provide immunity from borrower claims and its expansion to account for infirmities in the APOR calculation is appropriate.

Clearer Guidance on Rebuttable Presumption QMs to Facilitate Lending

Even if the points and fees and APOR issues are fixed as we suggest, MBA believes additional guidance from the Bureau is necessary for the market to provide reasonably priced rebuttable presumption QMs.

MBA appreciates that the Bureau provided some additional guidance in its final rule in this area. Specifically, the rule provides that consumers may show a violation and rebut the presumption of compliance for a QM where the APR exceeds the APOR by 150 bps or more by showing that, at the time the loan was originated, the consumer's income and debt obligations left insufficient residual income or assets to meet living expenses.

Guidance accompanying the rule also notes that the longer the period of time that the consumer has demonstrated actual ability to repay the loan by making timely payments, without modification or accommodation, after consummation or, for an adjustable-rate mortgage, after recast, the less likely the consumer will be able to rebut the presumption based on insufficient residual income.

While these points are useful, it would be far more useful in facilitating efforts to encourage lenders to originate rebuttable presumption loans if there were clear guidance about what is meant by residual income and what is meant by a good payment history. For instance, "residual income" can be calculated using Department of Veterans Affairs or several other standards. "Good payment history" is a vague and subjective standard without definition.

MBA has asked the Bureau to provide further guidance in this area and the Bureau has indicated it will not do so, urging instead that lenders use common sense to determine the sufficiency of residual income. While we agree with the CFPB that common sense is a critical part of any underwriting decision, it is not always the standard followed by counsel when an action is brought. Therefore, to give lenders and investors greater legal certainty, guidance is essential if QM rebuttable presumption loans are to be made in great numbers across the spectrum of qualified borrowers.

The Rules Must Be Aligned With Each Other

HUD's New Disparate Impact Rule Under the Fair Housing Act

HUD's recently finalized Discriminatory Effects or disparate impact rule under the Fair Housing Act typifies the need for the CFPB's ATR/QM rule to be aligned with other federal regulations.

HUD's rule expressly provides a legal basis for liability under the Fair Housing Act for a facially neutral mortgage lending or servicing practice that has a disparate impact or "discriminatory effect" upon a protected class even in the absence of any intention to discriminate.[2]

Yet rules implementing Dodd-Frank, including the ATR/QM rule and the forthcoming risk retention rule, will in fact tighten credit standards through facially neutral requirements and can be expected to lead to disparate outcomes for some categories of borrowers. Requirements for the QM, for example, include a 43 percent debt-to-income requirement or eligibility for Fannie Mae and Freddie Mac purchase or guarantee.

[2] 24 C.F.R. § 100.500.

HUD has issued no guidance on whether and to what extent a lender's policies in making only QM loans, or taking similar actions, in compliance with the ATR/QM requirements amounts to "legally sufficient justification" or business necessity that would avoid liability. Similarly, there is little guidance on assessing less discriminatory alternatives under the rule's burden shifting test in the context of complying with other federal requirements.

We support prohibition of illegal discrimination in mortgage lending under the Fair Housing Act. And while we have questioned the legal foundations underlying the disparate impact theory under the Fair Housing Act, if this rule is to apply, it is essential that it offer clarity on how the rule interacts with the ATR/QM rule and other government requirements.

On June 4, MBA, several other financial trade associations, and the U.S. Chamber of Commerce all wrote to CFPB Director Cordray and HUD Secretary Donovan setting forth these concerns and urging written guidance that makes clear that a lender will not be subject to disparate impact liability based on specific policies undertaken to avoid liability under the Dodd-Frank rules. A lack of guidance in this area will create a regulatory double bind for lenders and ultimately result in higher prices to account for risk and less available credit for consumers.

The Ability to Repay Rule's QM Should Be the Same as the Risk Retention Rule's Qualified Residential Mortgage (QRM)

Another key piece of aligning the rules in MBA's view is aligning QM and QRM definitions.

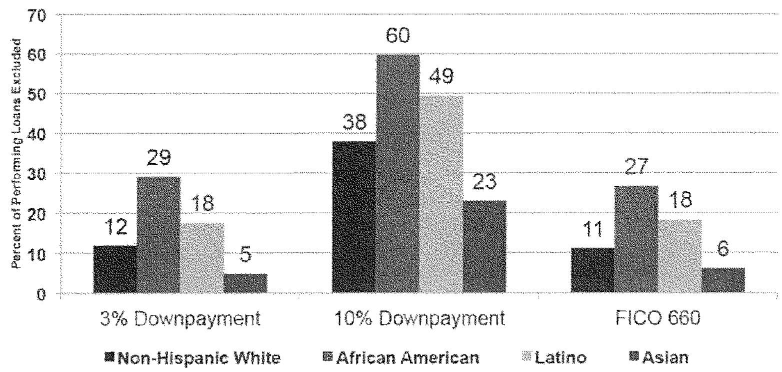
While the QM is the responsibility of the CFPB and the QRM is the joint responsibility of six financial regulators, excluding the CFPB, both provisions have at their heart the same objective. One seeks to outline the design of a sustainable mortgage as a means of satisfying the ability to repay requirements and the other provides an exception to the requirement for risk retention. Notably, Section 941 of the Dodd Frank Act, which establishes the QRM exemption, also requires that the QRM definition be no broader than the definition of QM.

Considering these points, MBA shares the view of an array of stakeholders that the definitions should be synchronized.

Regrettably, however, the QRM proposal issued in 2011 established the QRM in a manner that would serve an extremely narrow segment of the mortgage market for which few middle income families would be eligible. Unlike the QM, the QRM proposal contained a 20 percent down payment for purchase loans and even higher equity standards for refinances. In addition to these standards, the QRM proposal included minimum debt-to-income requirements that were far tighter than those in the marketplace. The proposal engendered a negative reaction from virtually every stakeholder in the consumer advocacy, lending and real estate communities.

Increasing Downpayments and Capping Credit Scores Will Disproportionately Impact Minorities

Percent of performing loans excluded from QRM mortgage market, alternate LTV and FICO definitions, by borrower race/ethnicity, 2004-2008 originations



Source: Roberto Quercia, Lei Ding, and Carolina Reid (2012). *Balancing Risk and Access: Underwriting Standards for Qualified Residential Mortgages*, Center for Community Capital Research Report, January 2012.

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Since the QRM rule was proposed, the QM rule has been finalized. While we have concerns that are discussed extensively above, we believe both definitions should be based on the QM.

As finalized, the QM definition provides strong underwriting, documentation and product standards that will demonstrably lower the risk of defaults consistent with the statutory requirements for the QRM. At the same time, the QM definition precludes the riskier features and products that likewise should be ineligible for QRM treatment. Finally, it does so without restricting credit to low- and moderate income families who no matter how worthy their credit lack the wealth for significant down payments.

There is no need for two different definitions of a sustainable loan. In fact, such variations will only increase costs and confusion to the industry and consumers. Aligning the QRM and QM standards would ensure that strong incentives for safe and sound lending are in place, while inviting the return of private capital and lower mortgage rates to the widest array of qualified families.

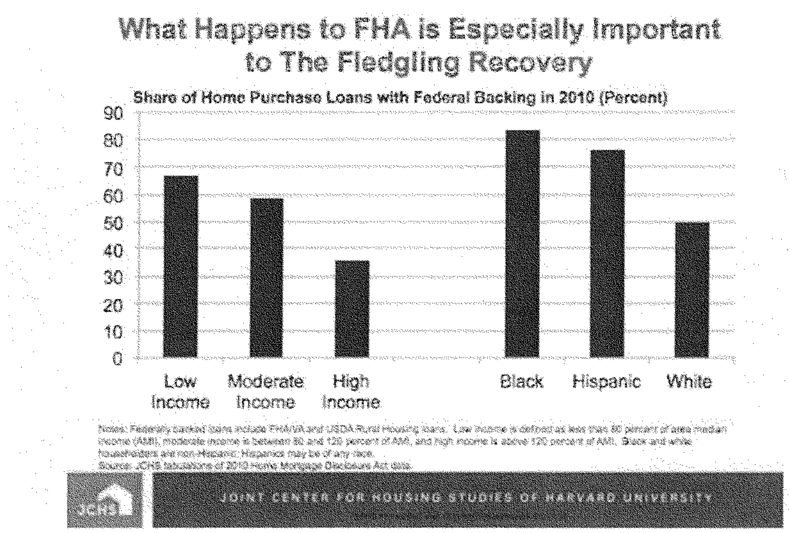
FHA and QM

The QM encompasses government loans including FHA loans. The CFPB's QM rule will govern FHA loans until FHA writes its own QM regulation, which is expected within the next several months.

Consumers would be better served if QM safe harbor loans were made available to more creditworthy borrowers by adjusting the APOR benchmark upward to 200-250 basis points. The rule's 150 basis points benchmark is particularly troublesome for FHA loans.

FHA's upfront mortgage insurance premium (MIP) has recently been increased. The MIP is included in the APR and consumes a substantial amount of the 150 basis points. Specifically, analysis from a major FHA lender suggests that the FHA's MIP changes will add 40 to 70 basis points to FHA APRs, depending on loan amount and LTV. This problem with the benchmark is further exacerbated by the fact that the PMMS underlying the APOR only includes conventional not government loans.

If the threshold is not at least expanded — and we urge it be expanded for all loans — the availability of FHA credit to first-time, minority, and low and moderate income borrowers will be jeopardized. The importance of FHA lending to underserved populations is depicted below:



For these reasons, it is vital that FHA's forthcoming QM rule include appropriate triggers for QM loans. In the interim, until FHA's QM rule takes effect, we hope Congress will urge the CFPB to adjust the metrics so FHA loans are not treated as rebuttable presumption QM loans.

Guidance and Time to Implement the Rules

As I indicated, implementing the ATR/QM rule along with the other rules issued in January is an enormous task that includes developing new policies and procedures, reengineering loan application and origination processes, building new systems and audit protocols, and training employees, to name just some of the many steps.

To aid in our work, the CFPB's efforts to provide implementation guidance are essential. In this regard, we appreciate that the Bureau has assigned an experienced professional to lead its implementation process and that Bureau representatives have participated in key industry conferences to facilitate stakeholder understanding of the rules. We also appreciate that the CFPB is consulting with lenders, technology providers and others to help operationalize the rules.

Going forward, we urge that questions be answered in writing and publicized widely. This will allow for standard or frequently requested interpretations to be widely known and clearly understood.

Finally, it is imperative that the CFPB be encouraged to make further refinements to the QM rule during the next few months. There are several areas, including the points and fees calculation, the small loan limits and the APOR/APR spread that should be addressed further.

We recognize there is concern at the Bureau about extending compliance deadlines beyond January 2014. We have, however, urged that the Bureau exercise its exemption authority as needed to provide additional time for compliance.

We urge Congress to encourage such an action by the CFPB as needed. Rigid adherence to time limits should not be allowed to dictate implementation if it will frustrate the interests of the consumers that the limits are designed to protect. The stakes are simply too high.

Conclusion

We appreciate the efforts of the subcommittee to examine these enormously important regulations. No matter how well intentioned these rules may be, we remain concerned that the ATR/QM rule harms competition and does not yet ensure credit opportunities to all qualified borrowers.

We urge your support of H.R. 1077 to revise the point and fees provisions and to adjust the small loan limits as needed.

I look forward to your questions. I also look forward to continuing to work with this subcommittee to ensure that our nation has a vibrant mortgage market for as many qualified borrowers as possible, for generations to come.

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NATIONAL ASSOCIATION OF REALTORS®

SUBMITTED FOR THE RECORD TO

THE UNITED STATES HOUSE OF REPRESENTATIVES COMMITTEE ON FINANCIAL SERVICES SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

HEARING TITLED

"EXAMINING HOW THE DODD-FRANK ACT HAMPERS HOME OWNERSHIP"

JUNE 18, 2013

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EQUAL HOUSING OPPORTUNITY

INTRODUCTION

Madam Chairwoman, Ranking Member Meeks, and members of the Subcommittee, I am Gary Thomas, President of the National Association of REALTORS® (NAR) from Orange County, CA. I have more than 35 years' experience in the real estate business and I am the Broker/Owner of Evergreen Realty in Villa Park, California. In 2001, I served as president of the California Association of REALTORS® and have had the honor of serving on NAR's Real Estate Settlement Procedures Act Presidential Advisory Group for a number of years. I thank you for the opportunity to participate in this hearing on behalf of the 1 million members of the National Association of REALTORS®. NAR represents a wide variety of housing industry professionals committed to the development and preservation of the nation's housing stock and making it available to the widest range of potential homebuyers.

In my testimony today, I will address several key issues regarding the Ability to Repay Qualified Mortgage (QM) rule. The Dodd-Frank Wall Street Reform Act established the QM as the primary means for mortgage lenders to satisfy its "ability to repay" requirements. NAR has been generally supportive of the Consumer Financial Protection Bureau's (CFPB or the Bureau) efforts to craft a QM rule that is not unduly restrictive and provides a safe harbor for lenders making QM loans. NAR has had policy supporting the idea that lenders measure a consumer's ability to repay a loan since 2005.

3% Cap on Fees and Points

However, Dodd-Frank also provides that a Qualified Mortgage (QM) may not have points and fees in excess of 3 percent of the loan amount. As currently defined by Dodd Frank and in the Consumer Financial Protection Agency's (CFPB) final regulation to implement the "ability to repay" requirements, "points and fees" include (among other charges): (i) fees paid to affiliated (but not unaffiliated) title companies, (ii) amounts of homeowner's insurance held in escrow, (iii) loan level price adjustments (LLPAs), and (iv) payments by lenders to correspondent banks and mortgage brokers in wholesale transactions.

As a result of this problematic definition, many loans made by affiliates, particularly those made to low- and moderate-income borrowers, would not qualify as QMs. Consequently, these loans would be unlikely to be made or would only be available at higher rates due to heightened liability risks. Consumers would lose the ability to choose to take advantage of the convenience and market efficiencies offered by one-stop shopping. H.R. 1077, "The Consumer Mortgage Choice Act," has been introduced by Reps. Huizenga (R-MI), Bachus (R-AL), Royce (R-CA), Stivers (R-OH), Scott (D-GA), Meeks (D-NY), Clay (D-MO), and Peters (D-MI) to address the inequitable treatment inherent in the fees and points calculation. Similar legislation (S. 949) has been introduced by Senators Manchin (D-WV) and Johanns (R-NE) in the Senate.

It has been argued that CFPB has the authority to fix this problem. The Bureau has partially addressed some of the original concerns with the counting of loan officer compensation towards the 3% cap. However, as the CFPB noted in their final rule and intimated in recent testimony, they do not believe they have the authority to fix the issue of affiliate charges and do not plan to address further other matters. For this reason, NAR believes that only Congress can fully rectify the law's discrimination against affiliates, small and mid-size lenders, community banks, and credit unions in the calculation of fees and points.

Key Components of H.R. 1077

The key components of H.R. 1077 include:

- The bill removes affiliate title insurance charges from the calculation of fees and points. The title industry is regulated at the state level and competitive. It does not make sense to discriminate against one type of provider, i.e. affiliates, on the basis of these regulated fees. To do so would only reduce competition and choice in title services and providers to the detriment of consumers. In a recent study of transactions by one real estate firm with affiliate mortgage and title operations, title and related charges were actually found to be $500 less than that of its unaffiliated competitors in the market.

  Furthermore, owners of affiliated businesses can earn no more than a proportionate return on their investment under the Real Estate Settlement Procedures Act (RESPA). RESPA also prohibits referral fees or any compensation at all for the referral of settlement services. As a result, there is no steering incentive possible for individual settlement service providers such as mortgage brokers, loan officers or real estate professionals. Since the Bureau now enforces RESPA and has enhanced authority under the statute, the Bureau has all the power necessary to prosecute kickback situations and other violations of RESPA. Instead of applying a double standard to affiliates, the Bureau should use its RESPA authority to ensure that both affiliated and unaffiliated companies of all sizes comply with RESPA.

- The bill removes a manner of counting fees and points that would unfairly discriminate against Mortgage Banking and Mortgage Brokerage entities by only counting as fees and points monies paid directly by the consumer to the originator, be they a broker or a mortgage bank loan officer. The Bureau partially addressed this issue in a recent rulemaking. However, NAR believes the legislative language remains necessary to ensure now and in the future that certain business models popular with consumers are not unfairly discriminated against in the calculation of fees and points.

- The bill removes from the calculation of fees and points Fannie Mae and Freddie Mac Loan Level Price Adjustments (LLPAs). This money is not revenue accruing to the lender. These adjustments are essentially risk based pricing established by the GSEs, and can sometimes exceed 3 points in and of themselves. Including these LLPAs would limit access to affordable mortgage credit to many borrowers or force borrowers into more costly FHA or non-QM loans unnecessarily.

- The bill removes from the calculation of fees and points escrows held for taxes and insurance. The tax-related language clarifies imprecise language contained in Dodd-Frank. In the case of insurance escrows, these escrows are held to pay homeowners insurance and can be a large amount. They are not retained by an affiliate, and cannot be retained under RESPA, since RESPA requires excess escrows to be refunded. While the CFPB has stated that both taxes and insurance escrows are not to be counted, their guide to the Ability to Repay rule and the language defining fees and points both clearly state that insurance is to be counted when affiliates are involved with the transaction. While we appreciate the Bureau's efforts to address this, NAR believes the legislative fix is tbe most certain way to avoid future confusion and legal risk.

Ascribing additional charges to the affiliated lender is clearly unfair and may in fact lead to greater costs for consumers or at the very least, increased consumer dissatisfaction and decreased consumer choice. Studies show that consumers see a significant benefit to having their real estate agent and broker at the lead in the transaction and using their affiliated businesses for key services such as mortgage and title insurance. In a 2010 Harris Interactive study conducted after enactment of Dodd-Frank, buyers said that using affiliates saves them money (78%), makes the home buying process more manageable and efficient (75%), prevents things from "falling through the cracks" (73%), and is more convenient (73%) than using separate services. The survey also showed that buyers who used affiliates tended to be more satisfied than those who did not. Finally, more than 50% of home buyers who were aware that a firm offered a full range of services reported that it positively impacted their decision to use a particular real estate agent and the firm (as opposed to no impact or a negative impact.) Without H.R. 1077, many of these buyers would lose that option.

This bill is essential to maintain competition and consumer choice in mortgage origination. Without this legislation, and based on surveys of large real estate firms with affiliates, one-quarter to as much as one-half of loans currently being originated would likely not be eligible for the QM safe harbor. Consequently, these loans would likely not be made or would be concentrated amongst the largest retail lenders whose business models are protected from the fees and point definition discrimination. Therefore, NAR believes that Congress should pass HR 1077 well before the "ability to repay" provisions take effect in January 2014 since lenders are likely to begin adjusting their systems in the fall of 2013.

OTHER AREAS OF CONCERN

43 Percent Debt to Income Limit (DTI)

Another area of concern with regard to the underwriting standards for QM will be jumbo loans with DTI in excess of 43% and other loans, particularly when the exception for GSE loans expires. For lower loan amounts, FHA and other government backed loans will be the only loans that will satisfy the QM safe harbor when DTI exceeds 43%. Even if the GSE exception is maintained, jumbo loans and non-GSE or government backed loans will be subject to the 43% DTI cap making them more costly or less likely to he made.

For jumbo loans in particular, the DTI cap could impose significant restrictions in high cost areas. High income borrowers are more likely to obtain jumbo financing. Because of their higher residual incomes in gross terms, they can afford to have a higher debt to income ratio. NAR fears that if the non-QM market does not emerge or is anemic, credit in high cost areas could be further restrained. Therefore, we support greater flexibility with regard to DTI limits and QM.

QM and Qualified Residential Mortgage (QRM)

NAR believes that, assuming the concerns with fees and points are addressed, the QRM (which does not require risk retention by securitizers) should be constructed to match the QM. Dodd-Frank establishes that the QRM can be no broader than the QM, but it does not say it cannot be substantially the same. NAR has conducted significant research and has determined that further imposition of downpayment requirements and tighter debt-to- income and credit standards will decrease access to credit and increase costs without creating substantial improvements in loan quality.

In addition to cost concerns, NAR believes that for regulatory compliance purposes and to ensure consistent and reliable securitizations, having the two standards mirror each other is advisable. It is simply far easier to apply one test to a loan than two. It would also prevent possible issues with creating another class of loans, i.e. those that are QM but not QRM, that might affect their overall marketability and cost.

For these reasons, Congress should support, and regulators should establish, a QRM that substantially mirrors the QM.

CONCLUSION

NAR supports a broad QM rule that does not discriminate against affiliates, smaller lenders, community banks, or credit unions. Furthermore, NAR supports a QM rule that gives consumers maximum choice in service providers. Finally, NAR supports a QM and QRM rule that does not needlessly cause credit to be more costly or unobtainable.

We are already in a tight credit environment. The QM and other rules effectively ban the types of products and processes that led to the mortgage crisis. Congress and the CFPB should improve the QM rule to ensure that consumers who have the ability to repay their loans will have the access to affordable credit they deserve.

NAR thanks the Subcommittee members for their attention to these issues. We look forward to working with Congress and the Administration on efforts to address the challenges still facing the nation's housing markets.

TESTIMONY OF

CHARLES A. VICE

COMMISSIONER

KENTUCKY DEPARTMENT OF FINANCIAL INSTITUTIONS

On behalf of the

CONFERENCE OF STATE BANK SUPERVISORS

On

"THE ABILITY-TO-REPAY AND QUALIFIED MORTGAGE STANDARD FINAL RULE"

Before the

FINANCIAL INSTITUTIONS AND CONSUMER CREDIT SUBCOMMITTEE

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

Tuesday, June 18, 2013, 10:00 a.m.

Room 2128 Rayburn House Office Building

INTRODUCTION

Good morning Chairman Capito, Ranking Member Meeks, and esteemed members of the Subcommittee. My name is Charles Vice, and I serve as the Commissioner of the Kentucky Department of Financial Institutions. I am also the Chairman of the Conference of State Bank Supervisors (CSBS).

I appreciate the work of this Subcommittee and the full Committee to examine the impact of the Ability-to-Repay Rule and the Qualified Mortgage (QM) on the financial services industry and consumers. I also appreciate the opportunity to participate in this important discussion.

CSBS is the nationwide organization of banking regulators from all 50 states, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands. State banking regulators supervise 5,271 state-chartered depository institutions, most of which are community banks. Additionally, most state banking departments regulate a variety of non-bank financial services providers, including mortgage lenders. For more than a century, CSBS has given state supervisors a national forum to coordinate supervision of their regulated entities and to develop regulatory policy.

As part of this work, state banking commissioners have devoted tremendous effort to examining the regulatory environment for community banks. Through the CSBS Community Bank Steering Group and our policy development committees, we have reviewed community bank regulation, supervision, and proposals to address the challenges facing community banks.[1] As a result of these efforts, state regulators have identified portfolio lending as a key opportunity for policymakers to ensure community banks' ability to contribute positively to the economic well-being of their local markets. While today's hearing centers around the ability-to-repay rule and issues such as rural counties and balloon loans, the broader issue is the problems posed by a one-size-fits-all approach to regulating portfolio-based lending by community banks.

THE COMMUNITY BANKING BUSINESS MODEL

In my 25 years as both a federal and state bank regulator, it has become abundantly clear community banks are vital to economic development, job creation, and financial stability. The unique characteristics of the community bank business model set these institutions apart from the largest, most complex financial institutions.

For instance, community banks make credit available to individuals in all corners of the United States, ranging from the largest city to small, rural communities. According to the Federal Deposit Insurance Corporation's (FDIC) Community Banking Study, community banks are almost three times more likely than their counterparts to operate a banking office outside a metro area.[2] In fact, community banks are the only banking presence in 629 counties in the U.S.[3]

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[1] CSBS has identified a series of specific community bank regulatory relief proposals targeted at the key regulatory challenges that we see for smaller institutions. The full list of these proposals is included as Exhibit A at the end of this testimony.

[2] FDIC Community Banking Study, 3-4 (December 2012). *Available at* http://www.fdic.gov/regulations/resources/cbi/study.html.

By ensuring access to credit throughout the United States, community banks support areas otherwise not serviced by the financial services industry and provide a stabilizing force for the broader economy through macroeconomic cycles.

Community banks also fuel America's small businesses by understanding the local markets in which their customers operate. According to the FDIC Community Banking Study, while holding only 14 percent of banking industry assets, community banks hold 46 percent of the banking industry's small loans to farms and businesses.[4] While the nation's largest banks are also engaged in small-business lending on a large scale, the types of small business loans originated by community banks vary significantly from the small business loans originated at the largest banks. By the nature of their scale, the largest banks rely heavily upon model-driven lending practices, which turn small business loans into commodities. This system allows for tremendous volumes of loan origination, but fails to allow for judgment and flexibility at the local level.

Community banks are able to offer individualized credit products because they utilize different lending techniques than the largest institutions, engaging in relationship lending that considers "soft" data that can be more qualitative than quantitative. This enables community banks to originate and hold loans customized for their customers, including mortgages that would not qualify for the secondary market. Community banks make these loans because the banks understand the property, borrower, and credit type. This approach to lending supports communities in good times and bad, as witnessed by the $36 billion increase in mortgages held in portfolio by community banks when the secondary market came to a grinding halt in 2008.[5]

PORTFOLIO LENDING

My fellow regulators, and perhaps everyone in this chamber, agree lenders should determine a borrower's ability to repay the loan before extending any form of credit. It is a simple tenet of lending that was overlooked as new securitization-based lending models developed. As such, an explicit ability-to-repay standard as a response to a structural flaw in the originate-to-distribute business model is logical, despite the fact such requirements should be an inherent part of every mortgage transaction. However, lenders that hold loans on their books are fully incentivized to ensure the borrower can meet the monthly obligations of a mortgage. As such, lenders that retain the full risk of a borrower's default should be presumed to have made a good-faith effort of determining repayment ability, and it is their regulator's responsibility to trust and verify this determination.

Loans held in portfolio should be regulated and supervised differently than those originated for sale to third parties.

State regulators have long supported a flexible approach to underwriting for institutions that retain mortgages in portfolio because interests are inherently aligned between consumers and

[3] FDIC Community Banking Study at 3-5.
[4] FDIC Community Banking Study at 5-1.
[5] The amount of 1-4 Family Loans held in portfolio by banks with less than $10 billion in assets increased over $36 billion from year end 2007 to 2008. FDIC Statistics on Depository Institutions (March 2013).

lenders that retain 100 percent of the risk of default. When the consumer defaults, portfolio lenders are incentivized to work with the borrower to fix the problem.

We were pleased to see the Small Creditor QM rule recognizes the portfolio lending business model by creating a regulatory framework that supports the retention of mortgages in portfolio by community banks. The Consumer Financial Protection Bureau (CFPB, or the Bureau) appropriately summarized the aligned interest between borrowers and lenders, stating portfolio lenders "have strong incentives to carefully consider whether a consumer will be able to repay a portfolio loan at least in part because the small creditor retains the risk of default."[6]

To memorialize the aligned interests of portfolio lending, the CFPB has conferred QM benefits on loans originated by "small creditors." Small creditors are defined as those institutions with less than $2 billion in assets and fewer than 500 mortgage originations annually who keep those mortgages in their portfolio. These small creditors will be given more flexibility in the underwriting process, will not be subject to the prescribed 43 percent debt-to-income ratio requirement in the standard QM, and will have a higher cost threshold for the levels of protection conferred by QM status. The standard QM confers safe harbor protection from liability for loans that cost less than 1.5 percent above the average prime offer rate, and a lower level of legal protection – a rebuttable presumption of compliance – for those that cost 1.5 percent or more above the average prime offer rate. Recognizing that funding for community bank portfolio lending can be more expensive than other market participants, the CFPB increased this threshold to 3.5 percent for the small creditor QM. This threshold increase appropriately accounts for differences in the community bank business model, giving portfolio lenders the flexibility they need to originate loans based on consumer needs.

The policy implications of this regulatory right-sizing are critical for local economies across the country. By instilling legal certainty, community bank portfolio lenders will be able to make individualized lending determinations based on the credit needs of their customers. This is crucial for markets and borrowers who do not fit standardized credit profiles, reassuring lenders that properly underwrite loans that they have adequate legal protections when operating outside of secondary mortgage market parameters.

By promulgating a smaller institution-focused rule that recognizes the difference between portfolio lending and the originate-to-distribute model, the CFPB has taken the first step in appropriately tailoring regulation to the community bank business models. The CFPB Small Creditor QM is a starting point for right-sizing regulations as they apply to community banks, and CSBS encourages both Congressional and regulatory policymakers to utilize the CFPB small creditor concept as a model when moving forward in the development of other laws and rules that impact the portfolio loans of small creditors, such as appraisals, escrow, and capital requirements.

[6] Ability to Repay Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6622, 6624 (January 30, 2013).

Balloon loans held in portfolio should be considered QMs if the creditor has considered the borrower's ability to repay on an amortized basis over the life of the loan.

The treatment of balloon loans is one example where regulation is taking a broad brush approach that disadvantages community banks. When used responsibly, balloon loans are a useful source of credit for borrowers in all areas. Properly underwritten balloon loans are tailored to the needs and circumstances of the borrower, including situations where the borrower or property is otherwise ineligible for standard mortgage products. Since the mortgage is held in portfolio, community banks must work to ensure that the product is tailored to take into consideration all risks associated with the credit in order to avoid default.

Some have suggested that adjustable rate mortgages (ARMs) provide a suitable substitute for balloon loans. While many community banks and borrowers utilize ARMs, they are not necessarily the better option for all consumers. Because banks can restructure the terms of a balloon loan more easily than an ARM, they are able to offer the consumer more options for affordable monthly payments, especially in a rising interest rate environment. As a regulator, I prefer that lenders and borrowers in my state have flexibility and options when selecting consumer products and mortgages. Consumers and borrowers should not be forced into a product because of regulations prompted by the deficiencies of another business model. The ability for institutions and consumers to make informed decisions on the best suited product for their circumstances, such as a balloon loan, is an important risk-mitigation strategy I would like to see preserved.

In the run-up to the mortgage crisis, much of the underwriting for the "exploding" 2/28 and 3/27 teaser loans did not include a consideration of the borrower's ability to repay over the life of the loan and relied on the faulty assumption that housing prices would continue to rise. This business model did not have the consumer and investor protections inherent in all loans held in portfolio. Unfortunately, in addressing the failure of these products, the Dodd-Frank Act failed to consider the ramifications for banks that make traditional balloon loans responsibly and hold them in portfolio. By limiting balloon loans to those made in rural areas, the ability-to-repay and QM standards final rule eliminates a consumer-enabling product from being originated by lenders who retain 100 percent of the risk of default by holding the loan in portfolio.

The CFPB has made an effort to limit the negative statutory effects on balloons held in portfolio by extending the time frame before the balloon loan restrictions take place, potentially offering Congress an opportunity to act on this issue. This ensures portfolio lenders have time to work through issues with existing balloons, but also allows policymakers the opportunity to ensure a useful tool is not permanently removed from a bank's toolbox. Community banks offer balloons to satisfy consumer needs and accommodate their customers on an ongoing basis, which should be recognized under law. Accordingly, CSBS supports creating a statutory Small Creditor QM and applying it to all loans held in portfolio, including balloon loans.

Absent a legislative change conferring QM status on balloon loans held in portfolio, the CFPB should establish a petition process to fix inconsistencies in the rural designation process.

Balloon loans are currently eligible for QM status if they meet the basic QM requirements and are originated in a "rural or underserved" area.[7] The CFPB has the responsibility for defining "rural" and "underserved." Originally proposed by the Federal Reserve, the CFPB adopted certain county characteristics under the USDA's Urban Influence Code to determine the definition of "rural."[8] Though the CFPB clearly put considerable thought and effort into this definition, including expanding the narrow Urban Influence Codes proposed by the Federal Reserve, it has produced some illogical results. This is hard to avoid when trying to establish one standard for categorizing every rural area in a country with 3,794,000 square miles and more than 300 million people. Indeed, there are several federal rural definitions, including those based on Census Places, Census Urban Areas, Metro Counties, Rural-Urban Commuting Areas, contiguous Urbanized Areas, and others.

No single definition gets it right because land and population characteristics are inherently local and cannot be dictated by formula. Accordingly, CSBS has proposed that the CFPB establish a process whereby an interested party can petition the Bureau to designate a certain county as "rural" for the purposes of the balloon QM requirements under current law.

State geography makes it difficult to issue a uniformly applicable definition of "rural" based on county characteristics. A comparatively small state in land area, Kentucky has the third most counties with 120, behind only Texas (254) and Georgia (159). This makes Kentucky difficult to quantify for purposes of defining "rural" via Urban Influence Codes, which essentially consider a county part of a metropolitan or micropolitan statistical area if it borders a county that has a city of 10,000 or more. Since there are comparatively more counties in Kentucky than other states, a single county can have up to seven neighboring counties, thereby increasing the likelihood the Urban Influence Code will not necessarily reflect the underlying characteristics of the county.

As currently defined by the CFPB rule, the average rural county in Kentucky contains 57 people per square mile. However, there are 12 counties considered non-rural that have 57 people per square mile or less, including Bracken, Hancock, McLean, and Trimble counties, all with fewer than 10,000 people.[9] Conversely, there are 32 rural counties with more than 57 people per square mile, including one with 215 people per square mile and a total population of 65,565. It is illogical that a "rural" county can have six times the number of people on aggregate and five times the number of people per square mile than a non-rural county with a smaller population. These are the types of results that occur when an inherently local issue like determining the characteristics of land areas is done by formula in Washington, D.C. and not by local officials.

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[7] 15 U.S.C. § 1639c(b)(2)(E)(iv)(I).

[8] The applicable Urban Influence Codes for the rural definition are all noncore counties and micropolitan counties not adjacent to a metropolitan area. 12 C.F.R. 1026.25(b)(2)(iv)(A). For more information on Urban Influence Codes, see http://www.ers.usda.gov/data-products/urban-influence-codes.aspx.

[9] All census numbers are based on the 2010 census, which is the source of the currently applicable Urban Influence Codes.

This is the case in many other states. For example, Wirt County, West Virginia is not considered rural because of its proximity to Parkersburg. Wirt County has one town, Elizabeth, 24 unincorporated communities, and only 5,717 people. In Massachusetts, the island counties of Nantucket and Dukes (home of Martha's Vineyard) are considered rural, but the considerably less commercial Franklin County is not. There are five more people per square mile in Franklin County than Nantucket, but the counties are on opposite ends of the Urban Influence Code scale.

The CFPB's approach also creates illogical results in states with fewer, larger counties. For instance, Nye County, Nevada is the third-largest county in the United States. Despite containing only 2.42 persons per square mile and being home to Yucca Mountain, once considered for a nuclear waste repository because of its remoteness, Nye is not considered rural because it neighbors Clark County, home of Las Vegas.

To remedy the inconsistencies of a blanket approach to the rural definition and in the absence of a statutory change, CSBS has suggested the CFPB adopt a petition process for interested parties to seek rural designation for counties that do not fit the Urban Influence Code definition – a step that is within the CFPB's current authorities. CSBS recommended this approach to the CFPB in a letter dated March 26, 2013.[10] We stand ready to work with the CFPB to implement a regulatory process to enhance their challenging task of characterizing over 3,000 unique counties.

MOVING FORWARD

If the regulatory framework for the ability-to-repay requirement is going to encompass all mortgage lending, it needs to have the flexibility to adapt to varying business models – from originate-to-distribute lenders, to large banks that originate mortgages in a more production-line fashion, to community banks that hold loans in their portfolios. The originate-to-distribute market and the standardized lending models of large banks provide an excellent source of mortgage credit. However, the scale of these operations requires that underwriting be standardized to support a volume-focused business. This approach precludes the individualized lending determinations performed by community banks, which make a case-by-case determination of repayment ability for loans held in portfolio.

It is our responsibility as state regulators to ensure community banks can offer flexible products to meet the needs of their local communities, and it is the responsibility of policymakers to create a legal and regulatory framework that permits flexibility where borrower and lender interests are aligned. The CFPB has created a framework to accommodate this lending model through their Small Creditor QM, and policymakers should look to this framework in any reform initiatives.

At its core, community banking is about aligning economic incentives between borrower and lender. Community bank portfolio lenders are incentivized to ensure payments can be made over the life of the loan because they retain the full risk of default. Because of this risk, I expect the institutions I supervise to determine repayment ability based on the borrower's income,

[10] The CSBS letter to the CFPB is included as Exhibit B at the end of this testimony.

assets, employment, credit history, and ability to pay other debts. These are time-tested practices that ensure banks are lending in a safe and sound manner that regulators review through the supervisory process. This process works and should be encouraged for all loans held in portfolio by community banks to ensure they can continue to meet the credit needs of their communities.

Although this testimony focuses on mortgages and the Ability-to-Repay and QM Standard, we see the potentially harmful consequences of a one-size-fits-all approach to regulation across many areas of basic community banking and rules and regulations. For instance, banks need increased levels of and enhanced quality capital, but the Basel III standards designed for globally systemic financial institutions should not also apply to a $200 million bank. By way of comparison, Citibank in New York and Deutsche Bank in Frankfurt are respectively 5,000 and 10,000 times larger than the local community bank in Flemingsburg, Kentucky, creating a drastically different scope and scale of risks. Similarly, proprietary trades should not have the benefit of the federal safety net, but small banks should not have to prove they comply with the Volcker Rule when they only engage in basic commercial bank activities. As public officials charged with ensuring these institutions are well run and serve the local communities in which they operate, it is important federal policy appropriately recognizes the community bank business model for these institutions to continue serving their markets.

Thank you for the opportunity to testify today. State regulators stand ready to work with Members of Congress and our federal counterparts to develop and implement a supervisory framework that continues to recognize the importance of our unique dual-banking system.

Exhibit A

CSBS SINCE 1902

CONFERENCE OF STATE BANK SUPERVISORS

Proposals for Community Bank Regulatory Relief
June 2013

As locally based and locally accountable regulators, State Banking Commissioners are committed to ensuring a diverse financial services and banking industry. CSBS and its members believe that community banks are a necessary part of this diverse system and key to ensuring locally accessible credit and financial services. CSBS and its members also are concerned about the challenges facing the community bank business model, particularly those challenges arising from regulation and supervision. As a result of the work of the CSBS Community Bank Steering Group, the CSBS Board of Directors, and the entire membership CSBS has developed this list of regulatory relief proposals focused on ensuring that regulation and supervision reflect the community bank business model.

1. The Law Should Ensure Regulations are Tailored for Portfolio Lending

   Banks that originate and hold consumer loans have an aligned economic interest with the borrower. These banks provide the capital to support the credit and live with the risk of non-performance. In some cases, the credit is tailored to the needs and circumstances of the borrower which may prohibit the loan from being sold on the secondary market. This is an important source of credit for consumers and small businesses. Therefore, regulations should be tailored in such a way that they support and do not impede portfolio lending.

2. Fair Lending Examination Procedures Must be Tailored to Recognize the Relationship Lending Model of Most Community Banks

   Many times it is not the statute that creates the problem but the interpretation, guidance, and the examination techniques utilized. Despite interagency examination guidelines and assurances of continued fair lending collaboration, the states have observed a drastic difference in how the three federal banking agencies treat community banks on these issues. Our Community Bank Steering Group has listed overzealous compliance/fair lending examinations as a major issue facing community banks.

   Application of one size fits all examination techniques and tools to community banks without regard for the use of judgment based on deep knowledge of local credit markets is not appropriate. For example, loans held in portfolio often are tailored to the needs and circumstances of the borrower. A fair lending analysis of community bank loans should capture the differences and nuances of how and why certain loans were made or why there may be a difference in terms.

Despite assurances to the contrary, we are seeing an examination approach that lacks recognition of the community bank business model. Institutions are abandoning certain products due to these examination practices. The result is that the consumer and small business person are forced to leave the banking system for alternative delivery of products at a higher cost.
In addition to requiring accountability through its oversight capacity, Congress should explore ways to recalibrate fair lending requirements to recognize the community bank approach to relationship-based lending. Supervisors must utilize their flexibility to look beyond statistical models to determine fair lending violations at community banks.

3. Remove the Rural or Underserved Definition for Balloon Loans

   Limitation of the rural or underserved standard to balloon loan qualified mortgages should be eliminated. Balloon loans should be treated under the basic small creditor Qualified Mortgage standard proposed by the CFPB.

4. Appraiser Qualifications for Certain 1-4 Family Loans

   Regulations regarding appraisals can curtail credit in smaller communities where there can be a lack of qualified appraisers or a lack of comparable sales. Congress should require regulations to accommodate portfolio loans for owner-occupied 1-4 family loans, recognizing the unique challenges to securing a qualified appraisal and the lender's proximity to the market.

5. Ensure State Supervisory Representation on Federal Regulatory Bodies

   The current FDIC Board does not include an individual with state regulatory experience as required by law. The FDI Act and Congressional intent clearly require that the FDIC Board must include an individual who has worked as a state official responsible for bank supervision. As the chartering authority for 74% of all banks in the U.S., state regulators bring an important regulatory perspective that reflects the realities of local economies and credit markets. Congress should refine the language of the FDI Act to ensure that Congress's intent is met and that the FDIC Board includes an individual who has worked in state government as a banking regulator.

   In creating the CFPB, Congress clearly recognized that the CFPB would touch a variety of state-regulated financial services providers, and Congress directed the CFPB to collaborate closely with state regulators across both bank and non-bank supervision. Should Congress choose to establish a CFPB governing board, it must include a member with state supervisory experience.

6. Revise the Dodd-Frank Act Creditworthiness Provisions

   Certain aspects of Dodd-Frank that require the federal regulators to remove references to credit rating agencies in their regulations have negative implications for permissible investments standards. Community banks will be required to perform more in depth analysis of investment options to demonstrate their investment grade status. Many community banks do not have to capacity to perform such analysis and may be forced to turn to expensive third party analysis or abandon certain investment options altogether. Many of these investments are local bond issues that provide critical support to schools and city and county governments. Congress should revisit the Dodd-Frank creditworthiness provisions to ensure this unintended consequence for community banks is resolved.

7. Application Decisions Related to Community Banks Should Not Set Precedent for SIFIs

   Community bank applications submitted to federal banking agencies for transactions such as mergers and capital investments can take an extended time to process because the agencies have to ensure the decision will not establish a precedent that could be exploited by larger institutions. Federal law could provide the necessary protection by stating that application decisions for banks below a specified size (perhaps $2 billion) do not establish a precedent for any institution designated as a SIFI (i.e., a bank holding company over $50 billion or a designated non-bank SIFI).
   To further address the length of time the agencies are taking to review these applications, the review and approval process for applications submitted by institutions below a certain size should be de-centralized with more final decision-making authority given to FDIC Regional Offices and the regional Federal Reserve Banks.

8. Deposit Insurance for Defined Transaction Accounts

   The expiration of the Transaction Account Guarantee program eliminated an option for community banks to serve local businesses during a time of continued economic uncertainty. To encourage businesses to bank with community banks, the FDIC should treat deposits in defined transaction accounts, such as payroll, as the deposits of the designated beneficiaries of the funds. As evidenced by deposit insurance for revocable trust accounts, the FDIC has the authority to apply pass-through insurance to defined transactions where relationships are fiduciary in nature, such as when payroll funds are placed in a transaction account for the benefit of explicit employees. This would ease business concerns and protect consumers by spreading deposit insurance to each employee's share of the sum set aside for payday.

9. Risk-Based Capital

   Congress should mandate a study (by GAO or another applicable body) that investigates the value and utility of Risk-Based Capital for smaller institutions. The study should seek to understand how risk weights drive behavior in the volume and type of credit a bank originates, as well as the burden of providing the necessary data for calculation of the ratios.

10. Concern about Delayed Recognition of Losses

    Certain proposals addressing banking relief over the last few years have included provisions, such as delayed recognition of commercial real estate losses, that manipulate accounting standards in a fashion which overstates the financial condition of banking institution. We have longstanding safety and soundness concerns about measures that delay recognition of losses and believe they should not be included regulatory relief bills in the future.

Questions? Please contact:
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Exhibit B

CSBS SINCE 1902

CONFERENCE OF STATE BANK SUPERVISORS

March 26, 2013

The Honorable Richard Cordray
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, D.C. 20552

Dear Director Cordray,

As the Consumer Financial Protection Bureau ("CFPB") prepares to implement balloon qualified mortgage and escrow requirements for rural creditors, the Conference of State Bank Supervisors ("CSBS") would like to take the opportunity to suggest an additional procedural mechanism for the CFPB to utilize when determining whether an area should be defined as "rural." To mediate the inconsistencies inherent in a nationwide rural classification system, CSBS recommends adopting a petition process whereby interested parties can petition the CFPB to make a determination that a specified and bounded area be considered rural for the purposes of Truth in Lending rural requirements.

County Designations Require a Flexible Rural Designation Alternative

Practically speaking, there is no single good manner to define "rural" in a country with 3,794,000 square miles and more than 300 million people. As a result, the rural designation will not be applied to areas inherently rural because states and county sizes vary significantly. For example, the third largest county in the United States, Nye County Nevada, has only 43,946 people over 18,159 square miles, or 2.42 persons per square mile. Due to its proximity to Las Vegas, Nye County is still considered a core county under the Urban Influence Code, thereby preventing it from being defined as rural for Truth in Lending purposes. This is evidenced by the fact that Nye is the site of Yucca Mountain, the Department of Energy's original proposed site for storing spent nuclear fuel because of its remoteness among other characteristics.

The variance in rural definitions stems beyond the Urban Influence Code. The United States Department of Agriculture Economic Research Service can generate nine different definitions of "rural" depending on land boundaries and population thresholds. This creates a myriad of "rural" possibilities, from Census Places with a population less than 2,500 people, to a definition based on Rural-Urban Commuting Areas. While these options do not use counties as boundaries, it is easy to see why the CFPB would use a metric that relies on counties – the Urban Influence Code – as the applicable land boundary. Every house must be in a county, which is an easily quantifiable area. However, the population of that county may vary significantly, as might the Urban Influence Code classification because of the surrounding populations.

To mediate these inconsistencies, a process should exist whereby an interested party could petition the CFPB for a county to be considered rural. Specified criteria could be required, such as:

- Census Places data
- Census Urban Area data
- OMB Nonmetro County designation
- Rural-Urban Commuting Area data
- USDA Business and Industry ineligible location data
- USDA Rural Housing program criteria
- Population Density
- Population per square mile

Considering the changing dynamics of population, it might be logical to have open submission periods for such a process, whereby submitted data can be compared so the results can be consistent for all lenders. This would also be logical given Urban Influence Codes are subject to change.

When definitions affect credit availability, there should be some opportunity to submit a case to the defining body arguing why an area should be considered the type of area excepted for responsible balloon loan origination. CSBS would be happy to assist in the streamlining of such a process and commits to supporting any effort by the CFPB to mitigate the rural definition issue.

Balloon Loans Are a Crucial Credit Product for Community Banks

As a policy matter, CSBS believes portfolio lending aligns the interests of consumers and lenders, warranting a regulatory framework that encourages more originate-to-hold lending. CSBS believes the rural requirement for balloon qualified mortgages and escrow will often limit this type of responsible credit origination. However, CSBS recognizes the CFPB has limited options under the statute, further supporting the petition process outlined above.

Balloon loans held in portfolio give consumers significant interest rate flexibility. Consumers will refinance balloon loans regularly when interest rates are attractive, and most community banks provide this service without fees. Banks are able to provide this service better with balloon loans than adjustable-rate mortgages because the terms are simpler. Indeed, system capabilities often prevent community banks from servicing ARMs. Further, current funding mechanisms make it easier for small creditors to match funding for balloon loans than adjustable rate mortgages, making this form of credit cheaper for the consumer.

Community banks often originate balloon products and hold the mortgage on their books, refinancing and satisfying customer needs on an ongoing basis. Community banks also originate mortgages based on cost structures that do not include escrow services, working with the borrower to make sure taxes, insurance, and other required payments are made in a timely manner. These considerations are size based, not population based, and rural requirements will have a significant effect on the responsible mortgage products offered in many states. While we appreciate the final rural definition is much broader than the definition proposed, there may be opportunity to accommodate certain areas where this credit should be available despite Urban Influence Code classifications.

The Market Effects of New Rural Designations Will be Negligible

By definition, the balloon qualified mortgage and escrow requirements are local in nature. The mortgages must be held on balance sheet by small creditors in specified areas. Accordingly, there can be no meaningful impact on the broader credit market by having a rural petition process for the balloon qualified mortgage and escrow requirements.

As the CFPB continues to implement its mortgage rules, CSBS stands ready to help in the process as it relates to state and local areas.

Thank you for your consideration,

John W. Ryan
President & CEO

cc:

Steven Antonakes, Acting Deputy Director
David Silberman, Associate Director, Research, Markets & Regulations
Meredith Fuchs, Associate Director, Legal, General Counsel

Statement of the Community Associations Institute

House Financial Services Committee
Subcommittee on Financial Institutions & Consumer Credit

"Examining How the Dodd-Frank Act Hampers Home Ownership"

June 18, 2013

By

Dawn Bauman
Senior Vice President, Government & Public Affairs
Community Associations Institute

Chairwoman Capito and Ranking Member Meeks, thank you for the opportunity for Community Associations Institute (CAI)[1] to submit comments for the record for the Financial Institutions and Consumer Credit Subcommittee hearing entitled, "Examining How the Dodd-Frank Act Hampers Home Ownership."

The Subcommittee's hearing focuses on the Consumer Financial Protection Bureau's (CFPB or the Bureau) Qualified Mortgage (QM) rule, which implements key mortgage lending reforms required by the Dodd Frank Act. The QM rule requires that mortgage originators reasonably verify borrowers have the ability to make payments under the terms of a mortgage loan before extending credit. The QM rule also mandates that terms and conditions of mortgage credit meet minimum consumer protection standards.

CAI members support mortgage lending and securitization reforms that ensure access to credit on reasonable terms for Americans who choose to live in a community association (condominium, cooperative, or homeowner association).[2] Alternatively, CAI members strongly oppose any aspects of new mortgage lending and securitization policies that treat homeowners choosing to live in community associations differently.

Support for Ability to Repay
CAI members strongly support the basic premise that lenders be required to verify a borrower has the ability to repay a mortgage loan, including all mandatory monthly mortgage-related obligations, before extending credit. CAI members also strongly support the Bureau's determination that assessments paid by homeowners to their homeowner association are mortgage-related obligations.

Homeowner assessments fund community governance, operations, and often essential municipal services. Examples of the activities and functions supported by community association assessments include maintenance of community infrastructure such as roads, bridges, and wastewater systems. Assessments also fund insurance and maintenance of common elements, community management and governance, utilities, and other critical community services.

When homeowners fail to fund their fair share of community costs, the association must look to other owners to close budget shortfalls. Often, the only option is for the

[1] Community Associations Institute is an international membership organization dedicated to building better communities. CAI and its more than 60 chapters provide education, tools and resources to the volunteers who govern communities and the professionals who support them. CAI's 32,000 members include community association volunteer leaders (homeowners), community managers, association management firms and other professionals who provide products and services to associations. CAI's vision is reflected in community associations that are preferred places to call home.
[2] All community associations have three defining characteristics: (1) membership is mandatory and automatic for all owners; (2) certain documents bind all owners to be governed by the community association; and (3) mandatory lien-based assessments are levied on each owner in order to operate and maintain the community association. There are three basic types of community associations: condominiums, cooperatives and planned communities.

community to increase assessment rates or to impose a one-time special assessment on owners. These options can jeopardize the financial viability of prudent borrowers by increasing mandatory housing costs. CAI members believe the ability to repay standard of the Dodd Frank Act will end this threat to both prudent borrowers and community associations.

Including association assessments in the QM rule's ability to pay standard promotes the community association model of housing and is reasonable public policy. Unfortunately, not all aspects of the Dodd Frank Act or the QM rule meet this standard.

Concern over Points & Fees Limitations
Throughout consideration of the Dodd Frank Act, CAI members expressed concern that well-intentioned reforms may prevent creditworthy borrowers from qualifying for mortgage credit. The Dodd Frank Act's three (3) percent limitation on points and fees for QM loans offers a good example of this concern about unintended consequences.

CAI members support the intent of Congress in limiting mortgage loan points and fees. Borrowers must be protected from hidden or excessive charges that are not related to the performance or purchase of a valid service or product or that do not otherwise directly benefit the borrower or the real estate being purchased. To protect borrowers, the Bureau must exercise restraint as a definition of the charges subject to the QM points and fees limitation that is too broad will prevent qualified borrowers from accessing credit on the best possible terms.

CAI members are concerned the CFPB has failed to strike the right balance between consumer protection and access to credit in the final QM rule. The Bureau has included secondary market fees that are assessed on condominium unit mortgages in the QM rule's three percent points and fees limitation.

Fannie Mae and Freddie Mac (the enterprises) assess Loan Level Price Adjustments (LLPAs) on each condominium unit mortgage the enterprises purchase or guarantee. By requiring these secondary market fees to be subject to the total points and fees cap for QM loans, the Bureau may force condominium unit borrowers into more expensive and restrictive mortgage loans.

Based on fee schedules published by the enterprises, a 75 basis points LLPA is assessed on all condominium unit mortgages, irrespective of the stability of the condominium project or the credit qualification of the individual borrower. The enterprises also assess a wide number of other LLPAs and other fees sometimes known as Adverse Market Delivery Charges. The application of the fees is cumulative, and total secondary market charges vary by borrower and property type.

By way of example, published LLPA schedules show that a well qualified condominium unit borrower approved for a mortgage with a loan to value ratio of 90 percent could face total secondary mortgage market fees equal to 2 percent of the loan balance.

Other scenarios provided by the enterprises show that LLPA and other charges could range as high as 4.25 percent, depending on borrower, collateral, and mortgage product features.

A borrower whose mortgage is subject to LLPAs must either pay higher points or a higher interest rate to offset secondary market costs incurred by the originator. Including these secondary market costs in the points and fees limitation increases the likelihood the mortgage will violate QM rule standards. In this instance, a borrower who meets the ability to pay test will be denied access to credit on the best possible terms not due to any defect of credit, but rather by arbitrary rule. Condominium unit owners and purchasers deserve access to credit on fair terms and the Bureau's final QM rule may prevent this outcome.

LLPAs are already having a market impact on condominium unit owners. CAI notes that the Mortgage Bankers Association has cited LLPAs and other secondary market charges as a barrier to refinancing condominium unit mortgages through the Home Affordable Refinance Program (HARP). CAI members are very concerned that the inclusion of LLPAs and other secondary market fees in the total limitation on points and fees will mean condominium unit mortgages will not meet QM rule requirements.

Further, as the QM rule is constraint on the QRM risk retention exemption, condominium loans may not be viewed in the secondary market as good candidates for securitization. This will dry up already tight sources of credit in the condominium mortgage market, devastate condominium unit owners who will face a lack of eligible buyers, and deny many would be first-time buyers homeownership opportunity.

Support for Increasing Points & Fees Limitations
CAI members strongly support efforts by this subcommittee and by the Congress to increase the three percent points and fees cap that governs both the QM and QRM standards. CAI members were disappointed the Bureau chose not to more fully revise the points and fees limitation in recent amendments to the QM standard and are concerned the Bureau may lack sufficient statutory authority to make necessary adjustments.

At the very least, implementation of the three percent points and fees limitation should be delayed either by the Bureau or by the Congress. If the Congress should determine that legislative action is required to remedy this inequity in treatment of condominium owners, CAI members believe Congress could usefully consider retaining the points and fees limitation as a consumer protection, but at levels that reflect the reality of mortgage origination and secondary market fees.

Again, thank you for the opportunity to provide comments to the Subcommittee as you examine this important housing policy. The Subcommittee's consideration of the community association housing perspective is critical to the 62 million homeowners living in America's 325,000 community association.

Consumer Mortgage Coalition

Written testimony of

The Consumer Mortgage Coalition

Before the

Subcommittee on Financial Institutions and Consumer Credit

of the

Committee on Financial Services
United States House of Representatives

"Examining How the Dodd-Frank Act Hampers Home Ownership"

June 18, 2013

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The Consumer Mortgage Coalition (the "CMC,") a trade association of national mortgage lenders, servicers, and service providers, is pleased to submit written testimony for the record for the Subcommittee on Financial Institutions and Consumer Credit, of the Committee on Financial Services of the House Representatives.

There are quite a few new consumer mortgage regulations being written and implemented today, covering both loan origination and loan servicing broadly. The Consumer Financial Protection Bureau ("CFPB") is trying to redesign mortgage regulations in a number of areas.

Overall, we support the CFPB's thoughtful approach to this redesign. The agency is listening to many views, and is striving to create regulations that resolve problems and that serve consumers and markets.

Title XIV of the Dodd-Frank Act required the CFPB to write several mortgage regulations, and set a schedule – these regulations were required to be final by January 21, 2013, and are required to become effective within a year after they become finalized. Regulations under Title XIV that are not required are not subject to this schedule.

I. <u>Recent and Pending Mortgage Rulemakings</u>

The CFPB is in the process of finalizing several mortgage rulemakings, some of them quite significant.

A. Ability-to-Repay Regulation

A significant rulemaking is the ability-to-repay regulation, also known as the qualified mortgage ("QM") rulemaking. This regulation requires creditors to verify and document a consumer's ability to repay a mortgage loan. Violations are subject to severe liability, known as "enhanced damages" under the Truth in Lending Act ("TILA").

1. There Are Three Basic Ways to Comply With This Regulation.

1) One compliance method is to make a QM loan at an annual percentage rate ("APR") less than 150 basis points over the average prime offer rate ("APOR"), a market measure of the rate on prime loans. (Small lenders have a higher threshold.) These loans enjoy a safe harbor from liability. GSE and FHA loans can qualify for this safe harbor if their APR is less than the 150 basis point spread over the APOR.

2) Another method is to make a "higher-priced" QM loan, which is a QM loan with an APR 150 basis points or more over the APOR. These loans do not have a safe harbor,

they have merely a rebuttable presumption of compliance with the ability-to-repay regulation. GSE and FHA loans can also qualify for this rebuttable presumption.

All QM loans, regardless of their APR, cannot have certain risky features, including an interest-only period, negative amortization, or a term of longer than 30 years. Balloon payments are permitted only on loans by certain small lenders, and prepayment penalties are restricted. Significantly, points and fees on QM loans are limited to three percent of the loan amount. The definition of points and fees is therefore significant.

3) A third method of complying with the regulation is to make a loan that is not a QM loan. The lender must still verify and document the consumer's ability to repay the loan, but the loan may have risky features and may have points and fees above three percent of the loan amount. Non-QM loans offer the lender neither a safe harbor from liability nor a rebuttable presumption of compliance.

Some aspects of the final regulation are helpful, including the safe harbor and new clarity in the definition of points and fees. However, the regulation still will unnecessarily constrain mortgage credit, because of the definition of points and fees, and because the regulation includes an undefined residual income standard, as discussed below.

2. *The Safe Harbor Solves a Problem*

The CMC was very pleased that the final ability-to-repay regulation has a safe harbor from liability for some loans. Without a safe harbor, lenders nationwide would have pulled back from the marketplace unnecessarily drastically because of the potential for enhanced TILA damages.

Enhanced TILA damages are not new under the Dodd-Frank Act. They have applied to so-called HOEPA[1] loans, a type of high-cost loan, for years. Lenders make almost no HOEPA loans as a result. According to the Government Accountability Office, for example:

> "Because of the associated penalties and liabilities, lenders have generally avoided making high-cost loans, and the secondary market for these loans has been negligible. Data collected under the Home Mortgage Disclosure Act (HMDA) indicate that in 2004 (the first year for which marketwide data on high-cost loans are available), lenders reported making 23,000 high-cost loans, which accounted for only 0.003 percent of all the originations of home-secured refinance or home improvement loans reported for that year. The number of reported high-cost loans rose to about 36,000 in 2005 but fell every year thereafter. In 2009, the most current year for which HMDA data are available, these loans numbered only

[1] HOEPA is the Home Ownership and Equity Protection Act of 1994, Pub. L. No. 103-325, §§ 151–158, 108 Stat. 2160, 2190-2198 (1994) (codified as amended in scattered sections of the Truth in Lending Act, 15 U.S.C. §§ 1601–1667f).

6,500, which, in aggregate, made up less than 0.1 percent of all the originations of home-secured refinancing and home improvement loans reported for that year."[2]

Lenders have historically been unwilling to make loans subject to enhanced damages in almost all cases. The Dodd-Frank Act applied enhanced TILA damages to loans that are not in compliance with the ability-to-repay regulation, so lenders need a safe harbor to be able to make any more than a handful of loans.

3. The Final Definition of Points and Fees is Clearer Than the Proposed Definition

The final regulation clarifies the definition of points and fees. While in the proposed regulation this definition was unclear in many areas, the CFPB has improved the clarity. One way the CFPB did so was to clarify that the amount of points and fees on a loan is known before the loan closes. This is critical because loans that have points and fees in excess of three percent of the loan amount are not QM loans, will not be qualified residential mortgage ("QRM") loans under the risk retention regulation, and because loans with points and fees above five percent are HOEPA loans.

Another area where the CFPB greatly clarified the points and fees definition concerns employee compensation. Unlike the proposed regulation, the final regulation excludes from points and fees compensation that a lender pays to its employees. This is important because quantifying compensation that relates to a specific loan would have been operationally quite difficult. It would have required analyzing retirement plan contributions, contingent commissions, compensation plans that are amended as a loan progresses through underwriting, and somehow tying this compensation to specific loans. The calculation would have been so complex that lenders would have needed to estimate points and fees very conservatively. This means lenders would have treated many QM loans as potential non-QM loans, and would have refused to make them.

4. The Definition of Points and Fees Inappropriately Distinguishes Affiliates and Nonaffiliates Without Regard to Consumer Protection

Although the definition of points and fees is improved, it will still prevent too many appropriate loans from being made. Points and fees include amounts paid to third parties, but only if the third party is affiliated with the lender. This is true even if the affiliate charges less than a nonaffiliate, thereby creating a perverse incentive to increase the cost to the consumer to stay below the three percent cap. This is unfortunate because affiliated business arrangements have been regulated for many years. Lenders must both: 1) disclose the affiliation; and 2) permit the borrower to elect a nonaffiliate. Given this

[2] MORTGAGE REFORM Potential Impacts of Provisions in the Dodd-Frank Act on Homebuyers and the Mortgage Market, pp. 56-57, GAO 11-656 (July 2011).

informed consumer choice, there is no consumer protection reason to alter the definition of points and fees based on affiliation. Rather, the Department of Housing and Urban Development ("HUD") has found that affiliated service providers can provide both lower costs[3] and the convenience of one-stop shopping.[4]

For these reasons, the CMC supports the Consumer Mortgage Choice Act, S. 949 and H.R. 1077, which would remove the distinction between affiliated and unaffiliated service providers for purposes of the definition of points and fees.

5. A Residual Income Standard is Needed

For non-QM loans, the lender must consider the borrower's debt-to-income ("DTI") ratio or the consumer's "residual income." Neither standard is defined – there is no maximum permissible DTI ratio, and there is no specified minimum acceptable level of residual income.

For rebuttable presumption QM loans, the borrower can rebut the presumption of compliance by showing that the borrower did not have sufficient "residual income or assets" to meet "living expenses," and "material non-debt obligations" of which the lender knew.

For both types of loans, residual income is not defined. There is no definition of "living expenses," no definition of which debts, expenses, or "material non-debt obligations" are relevant, and there is no standard at all of how much residual income is sufficient. The CFPB explains:

> The Bureau expects to study residual income in preparation for the five-year review of this [QM] rule required by the Dodd-Frank Act.[5]

We appreciate that the CFPB has not had time to conduct a study of the most appropriate residual income standard. However, the final ability-to-repay regulation applies a residual income standard for rebuttable presumption QM loans, and for loans that are not QM loans. For all these loans, lenders are held to a standard that they are unable to identify.

In other words, the expectation that lenders will be willing to make loans outside the QM safe harbor depends on lenders' willingness to be held to a standard of residual income that is entirely undefined. Lenders are subject to enhanced damages for noncompliance. Without a residual income standard, there is not much reason to believe there will be

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[3] HUD's proposed RESPA regulation, 59 Fed. Reg. 37360 (July 21, 1994).
[4] *HUD Economic Analysis* accompanying HUD's June 7, 1996 final RESPA regulation governing affiliated business arrangements.
[5] Section-by-section analysis to the final ability-to-repay / QM regulation, 78 Fed. Reg. 6408, 6528 (January 30, 2013).

loans outside the narrow safe harbor. This is unfortunate because the safe harbor is narrow – it must compensate the lender for the risks of the loan while keeping the APR low, and with points and fees no more than three percent. In other words, this regulation will largely constrain credit to borrowers with a strong credit profile.

We believe the CFPB should establish a residual income standard with which lenders can know how to comply. The Department of Veterans Affairs ("VA") has and uses a residual income test. We suggest that the CFPB should permit lenders use this test until the CFPB has time to study residual income standards and identify and implement a better standard, to the extent it finds a need to improve the VA standard. This approach would enable lending outside the limited QM safe harbor.

6. Lending Will Be Unnecessarily Constrained

Many believe lenders will be willing to make rebuttable presumption QM loans, or even non-QM loans. HOEPA loans have been extremely rare because they are subject to TILA enhanced damages. The Dodd-Frank Act increased the statute of limitations for enhanced damages from one year to three years, which increases the risk that lenders today are largely unwilling to incur.

Moreover, the Federal Reserve created a new class of loans, higher-priced mortgage loans ("HPMLs") in a 2008 regulation. TILA enhanced damages apply to these loans. HPMLs are loans with an APR that exceeds the APOR by 150 basis points, much like rebuttable presumption QM loans. Lenders make very few HPMLs because of the enhanced damages that attach to them:

> The 2011 HMDA data also include information on loan pricing. The 2011 data reflect the second full year of data reported under revised loan pricing rules, which determine whether a loan is classified as "higher priced." Lenders now report on loans with annual percentage rates (APRs) that are 1.5 percentage points for first lien loans and 3.5 percentage points for junior lien loans above the average prime offer rates (APORs), estimated using data reported by Freddie Mac in its Primary Mortgage Market Survey.
>
> The data on the incidence of higher-priced lending show that a small minority of first lien loans in 2011 have APRs that exceeded the loan price reporting thresholds. The principal exception was for conventional first lien loans used to purchase manufactured homes; for such loans 82 percent exceeded the reporting threshold in 2011. For conventional first lien loans used to purchase site-built properties, about 3.9 percent of the reported loans exceeded the reporting threshold (up from 3.3 percent in 2010). The incidence of higher-priced lending for FHA-insured loans on site-built properties (3.8 percent in 2011) is virtually the same as for conventional loans. The incidence of higher-priced lending for loans backed by VA guarantees is notably smaller than for either conventional or

FHA-insured loans; only about 0.4 percent of VA-guaranteed loans were higher priced in 2011.[6]

We believe the final QM regulation will constrain credit more than was intended and more than is appropriate. We therefore support, at a minimum, a clear and specific residual income standard that specifies what income, debt, and expense items are relevant, how lenders must quantify them, and the appropriate amount of residual income.

B. Risk Retention, HPML Loans, and FHA Premiums

The ability-to-repay regulation is best viewed in light of two separate regulations. One is the Dodd-Frank's risk-retention regulation, which is not yet final. It will require lenders or securitizers to retain five percent of the risk of securitized loan, unless the loan is a QRM loan. The definition of QRM loan may be "no broader" than the definition of QM loan. The cost of non-QRM loans will need to be high enough to compensate the lender for the cost of risk retention. Non-QRM loans will also be non-QM loans, and would subject the lender to enhanced TILA damages, if the lender is willing to make such a loan in the first place

For purposes of maintaining the solvency of the FHA insurance fund, FHA recently increased the mortgage insurance premiums on certain FHA loans, and now requires payment of the premium for a longer period of time. FHA insurance premiums are included in the APR. The FHA's recent increased and extended premiums will increase the APR, often above the HPML threshold, where lenders are rarely willing to go. This will drastically curtail FHA lending, especially on smaller loans. We do not believe this was the intent of either the HPML threshold or of the premium increase. Nevertheless, it will be the actual effect.

It may be advisable to revisit the overlap of the several rules that are designed to limit subprime lending. Taken together, the several regulations may unnecessarily constrain credit more than intended.

C. Servicing Regulations

The CFPB released two final servicing regulations in January 2013, which far exceed what the Dodd-Frank Act requires.

Generally, the CFPB regulations would institute a loss mitigation requirement based on existing Making Home Affordable programs HAMP and HARP. The regulations would

[6] Federal Financial Institutions Examination Council Announces Availability of 2011 Data on Mortgage Lending, Press Release (September 18, 2012) (footnote omitted).

require servicers to provide broad information upon request, and would redesign monthly statements.

While we support the overall goals behind the regulations, as originally released, the regulations need several issues resolved before servicers can implement the regulations.

For example, one of the servicing regulations finalized in January 2103 requires a notice to a borrower who becomes 45 days delinquent. At the same time, it prohibits servicers from taking certain action until the loan is 121 days delinquent. The CFPB tried to write the 121-day prohibition broadly to avoid loopholes. However, it prohibits is sending a "first notice or filing" until day 121, and this term is defined broadly enough to include the 45-day notice. The regulation appears to simultaneously require and prohibit the same notice.

Another example is that one of the final servicing regulations requires servicers to send notices to borrowers of the due date for a loss mitigation application, including four dates. Two of the dates are based on the number of days until a foreclosure sale, which dates the servicer may not be able to predict, and the dates may have already lapsed before the servicer sends the notice, without the servicer knowing so. This would require a notice to a borrower that is not helpful.

The information request provision in the final regulation is too broad, and would be a method of "back door" discovery without the benefit of a court's weighing the actual need for the information requested against the burden of producing it. The Dodd-Frank Act required the CFPB to define a valid qualified written request ("QWR") with which servicers must comply. Specifically, the Dodd-Frank Act intended to free servicers from the requirement to comply with abusive QWR "back door" discovery requests. The final regulation would revise and rename these abusive discovery requests, but would not remove them as Congress required. While we support the requirement that servicers supply relevant information to borrowers, the provisions as drafted would permit a continuing abuse without questioning the relevance of the information servicers would be required to produce.

The Dodd-Frank Act requires servicers to send monthly statements in most cases. However, the CFPB's regulation redesigned even the layout of the statements without first identifying a problem it wants to cure. Rearranging statement layouts is not a Dodd-Frank requirement, and we do not believe it should be required to be complete by the Dodd-Frank compliance date. It is burdensome, and any benefits have not been identified.

There are some areas where the periodic statement needs additional thinking. One concerns a requirement in a final regulation that servicers send monthly statements to borrowers in bankruptcy. We certainly support the policy of notifying borrowers of relevant information. However, the regulation does not have a separate statement for borrowers in bankruptcy. The same statement for a current borrower is in some ways irrelevant or misleading to a borrower in bankruptcy. Some bankruptcy courts will sanction servicers who even send a statement at all. While the policy of statements to bankrupt borrowers has merit, the statement would need to be specifically designed for the unique circumstances of bankruptcy. The CFPB needs to take time to design and test bankruptcy statements before requiring them.

The CFPB has said it will repurpose its servicing regulations this month.

D. HOEPA Rulemaking

In January 2013, the CFPB also finalized a HOEPA regulation. HOEPA prohibits certain lending abuses. The Dodd-Frank Act expanded its reach and lowered the thresholds that define a HOEPA loan. Virtually no HOEPA loans are made because of the liability they entail, so this rulemaking will be of limited effect. It is important to note, though that a HOEPA loans includes a loan on which points and fees exceed five percent of the loan amount. The definition of points and fees under the HOEPA regulation is largely the same as under the ability-to-repay regulation. (One difference is that the HOEPA regulation applies to open-end credit while the ability-to-repay regulation does not, so the HOEPA regulation defines the term for open-end credit.) If lenders become willing to make non-QM loans with points and fees above three percent, the HOEPA five percent cap would limit lending.

E. Loan Originator Compensation Regulation

The CFPB finalized a loan originator compensation regulation in January 2013. It will prohibit dual compensation to a mortgage broker, from both a lender and from a consumer. It will prohibit compensation to vary based on the terms of a loan (other than the amount of principal). This regulation is designed to prohibit yield spread premiums, much as a 2008 Federal Reserve regulation did.

F. Appraisal and Escrow Regulations

There are some additional new rulemakings that will have less impact than the regulations described above.

There are two new appraisal regulations. One requires lenders to provide a copy of each appraisal to borrowers, even if the loan never closes. Another requires appraisals, with an interior inspection, on certain loans, and a second appraisal if there is a risk that the property is being "flipped" – bought and quickly resold to an unsuspecting buyer at an inflated price.

There is also a new escrow regulation that exempts certain small creditors from the general requirement to establish escrow accounts on HPMLs. The impact of this rulemaking will be limited because of the scarcity of HPMLs.

These regulations are not as significant as other Dodd-Frank mortgage rulemakings, but they do require implementation resources.

II. Implementing the Many Regulations

The number of new mortgage regulations, coupled with the breadth of their impacts, will redesign the consumer mortgage industry in many or most areas. A look at the implementation process is therefore in order.

Normally, it is less burdensome to implement revised regulations all at one time rather than piecemeal. However, the CFPB is still revising some if the regulations it released only last January. The ability-to-repay regulation was revised on May 29, 2013. The servicing regulations are undergoing the broadest changes, which have yet to be proposed. Once the credit constraints implicit in the ability-to-repay regulation, and in the HPML restrictions as applied to the FHA premium increase, become apparent, regulations are likely to be revisited. For this reason, the luxury of implementing all the revisions at the same time is unavailable.

Some of the regulatory revisions are required by the Dodd-Frank Act. Others, including much of the servicing regulations, exceed the Dodd-Frank Act's requirements. We therefore believe it makes the most sense to implement those regulations that the Dodd-Frank Act requires by the statutory deadline of one year after the regulation becomes final. Regulations that the Dodd-Frank Act does not require should be implemented thereafter. The servicing regulations are not final – they will be reproposed shortly – and compliance with them by January 2014 should not be required.

III. Disparate Impact or Dodd-Frank Act?

The ability-to-repay and the upcoming risk retention regulations are designed to restrict mortgage lending to borrowers whose credit profile is very strong. If others are able to obtain loans at all, the price will be notably higher because of the cost of enhanced TILA damages under the ability-to-repay regulation, and because of the cost of risk retention for non-QRM loans.

At the same time, both HUD and the CFPB have made clear that they will view lending and servicing practices that have a disparate impact on classes of borrowers as illegal, even if the lender or servicer uses only neutral standards, such as the definition of a QM loan. The CFPB administers the Equal Credit Opportunity Act while HUD administers the Fair Housing Act, both of which apply to consumer mortgage lending.

The policy goals of applying a disparate impact theory of liability to mortgage lending and servicing is at cross purposes to the policy goals behind the ability-to-repay regulation, the risk-retention regulation, and the definitions of QM and QRM loans.

The industry needs substantial guidance on how to comply with two opposing policies. We recommend that a lender that elects to restrict its lending to only QM loans, or substantially only to QM loans, should not be subject to disparate impact liability. The lender in this case is complying with a federal policy that was a major hallmark of the Dodd-Frank Act mortgage reforms – the ability-to-repay and QM standard. Compliance with the a federal standard under one set of laws should not create liability under a separate body of law.

IV. Conclusion

The CMC appreciates the attention of this Subcommittee to the redesign of consumer mortgage lending under the Dodd-Frank Act.

Attached are two lists of guidance the CMC and other trade associations have submitted to the CFPB in connection with the origination and servicing rulemakings. These provide a more detailed picture of the types of issues the industry is handling in implementing the new regulations.

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AMERICAN FINANCIAL SERVICES ASSOCIATION
CONSUMER MORTGAGE COALITION
MORTGAGE BANKERS ASSOCIATION

GUIDANCE REQUESTS for SERVICING REGULATIONS to the BUREAU OF CONSUMER FINANCIAL PROTECTION

Working Document
June 3, 2013

Table of Contents

140

142

GENERAL MATTERS

TOPIC	ISSUE	RECOMMENDATION
1. Effective Dates	The Dodd-Frank Act requires a January 2014 effective date for required rules, but some aspects of the final servicing rules exceed the required rules. Mortgage servicers and lenders are currently implementing an enormous volume of new, and very comprehensive, set of regulatory amendments. More are yet to come. The industry must acknowledge the possibility that compliance by the January 2014 dates may not be possible.	We recommend that the CFPB discuss with industry member and representatives how to manage the implementation dates.
2. Small Servicer Definition, § 1026.41(e)(4)(ii)	The Regulation Z small servicer definition, at § 1026.41(e)(4)(ii), is incorporated into Regulation X by §§ 1024.17(k)(5)(iii) and 1024.30(b)(1). The definition provides: "(ii) *Small servicer defined.* A small servicer is a servicer that either: (A) Services 5,000 or fewer mortgage loans, for all of which the servicer (or an affiliate) is the creditor or assignee; or (B) Is a Housing Finance Agency, as defined in 24 CFR 266.5." For this purpose, does the word "assignee" refer to an assignee of the loan, the servicing, or either? If it refers only to the loan, the definition would be extremely narrow.	We request clarification of the term assignee in § 1026.41(e)(4)(ii). We also request clarification of the definition in the case of a small servicer that acquires servicing in a merger or acquisition of the creditor or assignee.
3. Definition of Business Day	The definition of business day is not the same in Regulation X and Z. The revised Regulation X frequently uses the term "days (excluding legal public holidays, Saturdays, and Sundays)." Regulation Z defines two types of business days, general and specific:	We request clarification that, under Regulation X, servicers can elect to treat Patriots' Day as a legal public holiday.

TOPIC	ISSUE	RECOMMENDATION
	"*Business day* means a day on which the creditor's offices are open to the public for carrying on substantially all of its business functions. However, for purposes of rescission under §§ 1026.15 and 1026.23, and for purposes of §§ 1026.19(a)(1)(ii), 1026.19(a)(2), 1026.31, and 1026.46(d)(4), the term means all calendar days except Sundays and the legal public holidays specified in 5 U.S.C. 6103(a), such as New Year's Day, the Birthday of Martin Luther King, Jr., Washington's Birthday, Memorial Day, Independence Day, Labor Day, Columbus Day, Veterans Day, Thanksgiving Day, and Christmas Day." Section 1026.2. Maine and Massachusetts, but not other states, observe Patriots' Day on the third Monday in April, when federal and state offices as well as many businesses are closed.	
4. Mailing as Delivery, § 1024.11	The new rule did not amend § 1024.11, which provides: "The provisions of this part requiring or permitting mailing of documents shall be deemed to be satisfied by placing the document in the mail (whether or not received by the addressee) addressed to the addresses stated in the loan application or in other information submitted to or obtained by the lender at the time of loan application or submitted or obtained by the lender or settlement agent, except that a revised address shall be used where the lender or settlement agent has been expressly informed in writing of a change in address." This does not mention servicers, yet servicers need to deliver disclosures to borrowers. The lack of mention of servicers, by negative	We suggest that § 11 be revised to read: "The provisions of this part requiring or permitting mailing of documents shall be deemed to be satisfied ~~by placing the~~ **when the** document **is placed** in the mail **or with a private delivery service** (whether or not received by the addressee) addressed to the address~~es~~ **obtained by the lender, settlement agent, servicer, or other party making the disclosure, as the appropriate delivery address. If the lender, settlement agent, servicer, or other party making the disclosure, receives notice of a change in that address, it must begin using the new address within a reasonable amount of time, which shall not be less than five specific business days.** ~~stated in the loan application or in other information submitted to or obtained by the lender at the time of loan application~~

146

GENERAL MATTERS

TOPIC	ISSUE	RECOMMENDATION
	implication, could be read to mean that servicers who mail disclosures have not delivered them until they are received, which is not the intent and would be unworkable because it is difficult to track when mail arrives or is received. The appropriate delivery address may not be the address "submitted to or obtained by the lender" and may not be a revised address of which "the lender or settlement agent has been expressly informed[.]" A servicer may be notified of a change of address, then later transfer the servicing to a new servicer. The new servicer will have the correct address but may not have received notice of a *change* of address. The regulation in some places provides that a servicer delivers a disclosure by putting it in the mail. *See* §§ 7(a)(2) and (b)(2); § 37(c)(1)(i); 37(d)(1); 37(e)(1)(i); 37(e)(5). However, in some places the rule is silent about whether a servicer has delivered a disclosure by mailing it. *See* § 34(b); 37(g)(2); and §§ 35 and 36.	~~or submitted or obtained by the lender or settlement agent, except that a revised address shall be used where the lender or settlement agent has been expressly informed in writing of a change in address."~~ Similar language in Regulation Z would be helpful.
5. UDAAPs		Compliance with Regulation X, Regulation Z, and their commentaries should in no circumstances be an unfair and deceptive act or practice ("UDAP") under state or federal law or a UDAAP under Dodd-Frank §§ 1031(a) or 1036(a)(1)(B).
6. Presumed Consent to Electronic Statements, Regulation Z Comment 41(c)-4	Regulation Z's comment 41(c)-4 provides: "Any consumer who is currently receiving disclosures for any account (for example, a mortgage or checking account) electronically from their servicer shall be deemed to have consented to receiving e-statements in place of paper statements."	This is helpful. We recommend applying this deemed consent to all disclosures under Regulations X and Z.

SERVICING – REGULATION X

TOPIC	ISSUE	RECOMMENDATION
Escrow Accounts, § 17		
7. Advancing premiums, § 17(k)(5)	Section 17(k)(5) provides: "(i) *In general.* Except as provided in paragraph (k)(5)(iii) of this section, with respect to a borrower whose mortgage payment is more than 30 days overdue, but who has established an escrow account for the payment for hazard insurance, as defined in § 1024.31, a servicer may not purchase force-placed insurance, as that term is defined in § 1024.37(a), unless a servicer is unable to disburse funds from the borrower's escrow account to ensure that the borrower's hazard insurance premium charges are paid in a timely manner. (ii) *Inability to disburse funds.* (A) *When inability exists.* A servicer is considered unable to disburse funds from a borrower's escrow account to ensure that the borrower's hazard insurance premiums are paid in a timely manner only if the servicer has a reasonable basis to believe either that the borrower's hazard insurance has been canceled (or was not renewed) for reasons other than nonpayment of premium charges or that the borrower's property is vacant." The definition of hazard insurance includes both flood and non-flood hazard insurance. Section 31. Suppose a servicer escrows for flood, but not any other hazard insurance, the loan is more than 30 days overdue, and the non-flood insurance premium is due. Must the servicer use the funds escrowed for	We request clarification that because the servicer is not authorized to pay the non-flood bills and the non-flood hazard insurance is not escrowed, the servicer should not use the flood insurance escrows for non-flood/non-escrowed items. We request clarification that if a servicer escrows for insurance that the servicer does not require, no advances are required for that nonrequired insurance. If there is ultimately a foreclosure and there are insufficient funds to reimburse the servicing advances as well as pay the accrued interest and principal balance, the investor will likely disallow the advanced premiums. It seems reasonable that when the borrower becomes delinquent, if any of the escrowed coverage is extra or the servicer can force place coverage for an amount less than the escrowed amount but still provide the minimum investor-required coverage, the servicer should not be obligated to continue to advance for the borrower's optional excess coverage.

TOPIC	ISSUE	RECOMMENDATION
	flood insurance premiums to pay for a different insurance policy? A borrower may request an escrow for insurance on the property that the servicer does not require.	
Scope, § 30		
8. Qualified lender, § 30(b)(3)	Section 30(b)(3) excludes from the scope of Subpart C: "A servicer with respect to any mortgage loan for which the servicer is a qualified lender as that term is defined in 12 CFR 617.7000." 12 C.F.R. § 617.7000 provides: "*Qualified lender* means: (1) A System institution, except a bank for cooperatives, that makes loans as defined in this section; and (2) Each bank, institution, corporation, company, credit union, and association described in section 1.7(b)(1)(B) of the Act (commonly referred to as an other financing institution), but only with respect to loans discounted or pledged under section 1.7(b)(1)."	We request clarification that this refers to servicers that are qualified lenders subject to Farm Credit Administration regulations. We request clarification whether the exclusion, for other financing institutions, applies only to loans that are loans "discounted or pledged" under § 1.7(b)(1).
Definitions, § 31		
9. Exceptions to the definition of loss mitigation option, § 31	Section 31 defines loss mitigation option as: "[A]n alternative to foreclosure offered by the owner or assignee of a mortgage loan that is made available through the servicer to the borrower." The second comment numbered 31-1 explains:	These types of workouts do not require a full review of the borrower's financial condition, so the § 41 protections, with a 30-day review period, are not necessary. These workouts may begin or be complete before day 36 of a delinquency, so the § 39 early intervention requirements should not apply. They also may be complete before day 45 of a delinquency so that the § 40 continuity of contact procedures should not apply. Servicers should have full flexibility to arrange payment plans with borrowers, rapidly when a full financial review is

TOPIC	ISSUE	RECOMMENDATION

	"Loss mitigation options include temporary and long-term relief, including options that allow borrowers who are behind on their mortgage payments to remain in their homes or to leave their homes without a foreclosure, such as, without limitation, refinancing, trial or permanent modification, repayment of the amount owed over an extended period of time, forbearance of future payments, short-sale, deed-in-lieu of foreclosure, and loss mitigation programs sponsored by a locality, a State, or the Federal government."
	
	This definition appears all-inclusive. Section 41 applies a number of procedural requirements for loss mitigation actions, and subjects servicers to private rights of action for alleged noncompliance. It is important that the definition of loss mitigation not be overbroad so that servicers will have flexibility to work with borrowers without having to take into account the cost of litigation risk for offering loss mitigation options.
	
	There are a number of workouts servicers routinely offer that do not rise to the level of needing formal § 41 procedures. Examples include:
	1. A borrower refinances, such as at a lower rate, lower UPB, or for a longer term, with the current servicer or its affiliate.
	2. On a current loan, a servicer unilaterally lowers the interest rate or converts an ARM loan to a fixed rate loan to prevent a potential default. The servicer has no need to review the borrower's financial condition.
	3. A borrower without an escrow fails to pay property taxes, so the servicer pays the taxes and permits the borrower to repay the taxes over time because the borrower claims inability to pay the taxes in a lump sum. The servicer does not necessarily review the borrower's
		unnecessary. These loan workouts do not need to go through the waterfall process because they are simple agreements, although § 41(e)(1)(i) would require considering the borrower for "all loss mitigation options available[.]"
		
		We recommend that the definition of loss mitigation option be revised to exempt the following:
		
		• Loan originations, whether or not related to resolving or preventing a default.
		• An adjustment that fixes or lowers the interest rate, or both, for the life of the loan, without extending the loan term or capitalizing any arrearages, at no charge to the borrower.
		• An agreement by which the borrower may pay the servicer for any mortgage-related obligations, as defined in § 1026.43(b)(8) [in the ATR rule, including taxes, insurance, condo and similar fees; ground rents; and leasehold payments] after they are or were due.
		• An agreement that permits the borrower to pay any portion of the loan payments at a date later than originally scheduled.
		  o *See*, for example, the Fannie Mae Guide, § 403, covering a number of borrower-specific situations in which "the servicer can agree to reduce or suspend the borrower's monthly payments for a specified period. Forbearance may be offered by itself or in combination with other foreclosure prevention alternatives, such as a combination of forbearance and a repayment plan." Forbearance plans are typically for six months, with longer plans requiring Fannie Mae approval. Servicers may be required to consider forbearance options, § 403.02.02.
		  o *See also* the Fannie Mae Guide § 404, covering repayment

TOPIC	ISSUE	RECOMMENDATION
	financial condition because the increase in periodic payments is relatively small and the borrower wants to remain in the home. 4. A borrower who has missed, or is about to miss, one payment or a few payments because of a unique event works out an arrangement with the servicer. The agreement may involve repayment over time, either currently or in the future, depending on the borrower's specific situation. The servicer does not review the borrower's financial condition as it would with a formal modification. Such agreements are often reached over the phone. Flexibility is critical to the success of these workouts because every situation is different.	plans, which are typically 12 to 18 months. Servicers may be required to consider repayment plans for temporary hardships. § 404. o Forbearance and repayment plans are less formal than modifications, typically require less documentation, and may be oral. The flexibility they offer can prevent unnecessary foreclosures. We also recommend that the definition of delinquency, for periodic statement purposes, in § 1026.41(d)(8), be limited to delinquencies that are not subject to an agreement with the servicer to resolve, repay, or otherwise work out the delinquency. In examples 3 and 4, the loan is technically delinquent although the servicer does not follow normal collection procedures. As long as the borrower continues to make payments as agreed with the servicer, there should be no need include delinquency information related to the workout in the periodic statement under § 1026.41(d)(8) because it will be covered by the agreement with the borrower. In addition, the § 1026.41(d)(8) information is not designed for examples 3 and 4. It requires disclosure of: • The date the consumer became delinquent. In examples 3 and 4, this will not matter to the borrower because the servicer has agreed not to pursue the delinquency. • Risks if the delinquency is not cured. In examples 3 and 4, this is not relevant because the servicer has agreed not to pursue the delinquency. • An account history showing the amount due from each billing cycle. Again, this is not relevant. The consumer needs to know how much

TOPIC	ISSUE	RECOMMENDATION
		to pay in the future, not which billing cycle it was "due." The amount to pay is set out in the agreement with the servicer. When the payment is "due" has changed, so the periodic statement would be misleading.
10. Definition of loss mitigation application, and time for verifying whether an agent is authorized to act for borrower, comment 31-1	Comment 31-1 provides that a loss mitigation application may be submitted by a borrower's agent, and that the servicer may undertake reasonable procedures to determine if a person that claims to be an agent of a borrower has authority from the borrower to act on the borrower's behalf.	Servicers have duties based on the date they receive a loss mitigation application. When an agent is involved, servicers should not be deemed to have received an application until they have had a reasonable amount of time to verify any agent's authority. The permitted time should not run while the servicer is waiting for a response to questions related to, or for documentation about, the agent's authority. This recommendation is the same treatment in comments 35(a)-1 and 36(a)-1, relating to the time to respond to error assertions and information requests. Those comments permit servicers to treat the error assertion or information request as received "[u]pon receipt of such documentation" from the borrower that the agent has authority to act on the borrower's behalf. It is also similar to Regulation Z comment 36(c)(3)-1, which permits creditors to verify the authority of an agent who requests a payoff statement before the time for delivering a payoff statement begins to run.
Servicing Transfers, § 33		
	See also § 38(b)(4), which covers servicing transfers.	
11. Appropriate mailing address, comment 33(b)(3)-1	Comment 33(b)(3)-1 provides: "A servicer mailing the notice of transfer must deliver it to the mailing address (or addresses) listed by the borrower in the loan documents, unless the borrower has notified the servicer of a new address (or addresses) pursuant to the servicer's requirements for	We recommend revising the language as follows: "A servicer mailing the notice of transfer must deliver it to the mailing address (or addresses) listed by the borrower in the loan documents, unless the borrower has notified the servicer**, lender, or a prior servicer** of a new address (or addresses) pursuant to the

152

TOPIC	ISSUE	RECOMMENDATION
	receiving a notice of a change of address." It is possible that a prior servicer, rather than a borrower, provided the change-of-address notice to the servicer who is mailing a notice, or that the borrower provided the change-of-address to a lender.	servicer's, **lender's, or prior servicer's** requirements for receiving a notice of a change of address."
12. Payments incorrectly sent to transferor, § 33(c)(1)	For 60 days after the transfer effective date, timely payments sent to the transferor "may not be treated as late for any purpose." § 33(c)(1). The transferor must either send the payment to the transferee or return it to the borrower with notice of the proper recipient. § 33(c)(2). The requirement that the transferee treat the payment as timely assumes that the transferee is aware of the payment, but this will often not be the case, at least for a few days after the transferor mails the payment. Comments 33(c)(1)-2 and 39(a)-1.iii both seem to acknowledge this. Borrowers who receive the returned payment, even with clear instructions on where to send it, may not forward the payment immediately, especially if they are under financial strain. Or, the borrower may be away from home and not realize the payment was misdirected, and would not know at least to call the servicer. Comment 33(c)(1)-2 provides that a transferee's "compliance" with § 39 (early intervention) during the 60-day period does not constitute treating a payment as late for purposes of § 33(c)(1).	To the extent the transferee has no reason to know a payment was timely sent to the transferor, has not received it, and acts as if the payment was not received, the transferee should not be held in violation of any law, policies or procedure under § 38, or any UDAP or UDAAP law. A transferee should be required to treat only one misdirected payment from the same borrower as timely. There is no need to notify borrowers repeatedly of the same information. One misdirected payment may be an error, but the second one likely is not. The borrower may assume that the transferor will not cash the check, meaning mailing a check that would bounce is a method to avoid payment. The requirement that the transferee treat a payment as timely even when the servicer has not received it should never apply to any of the servicer's duties to investors, it should only apply to the servicer's duties with regard to the borrower. We recommend a comment making this clear. Comment 33(c)(1)-2 talks of compliance with § 39 with respect to timely payments. Section 39 does not apply in the absence of a delinquency, and the concept of compliance with the inapplicable is confusing. It would be clearer to replace "compliance" with "actions based on § 1024.39[.]"

TOPIC	ISSUE	RECOMMENDATION
13. Preemption, § 33(d)	Section 33(d) preempts state laws that require servicing transfer notices.	It should also expressly preempt any federal or state UDAP laws, and UDAAP laws under Dodd-Frank §§ 1031(a) or 1036(a)(1)(B).
Escrow Refunds, § 34		
14. Payment of a loan in full, § 34(b)	Section 34(b) requires escrow refunds after "payment of a mortgage loan in full[.]" After a short sale, deed-in-lieu, or sale-leaseback, whether the loan is paid "in full" may not be clear, especially in states that do not permit deficiency judgments.	When a servicer, assignee, or both agree with a borrower or borrowers on a short sale, deed-in-lieu of foreclosure, sale-leaseback, or similar nonretention foreclosure alternative, whether any escrow refund is required should be determined by that agreement.
Error Assertions, § 35		
15. Annual escrow statements available on demand at any time, comment 35(a)-2	Comment 35(a)-2 provides: "A servicer should not rely solely on the borrower's description of a submission to determine whether the submission constitutes a notice of error under § 1024.35(a), an information request under § 1024.36(a), or both. For example, a borrower may submit a letter that claims to be a 'Notice of Error' that indicates that the borrower wants to receive the information set forth in an annual escrow account statement and asserts an error for the servicer's failure to provide the borrower an annual escrow statement. Such a letter may constitute an information request under § 1024.36(a) that triggers an obligation by the servicer to provide an annual escrow statement." The obligation to provide annual escrow statements is triggered by RESPA § 10(c)(2)(B) and by § 1024.17(i). The comment quoted seems to imply that a borrower can send in a request for an annual escrow statement, that is not an error assertion, and that the information request "triggers" an obligation to send an annual escrow statement. This seems to imply that borrowers have the right to receive annual escrow statements monthly.	We request clarification that an information request that does not assert an erroneous annual escrow statement does not trigger a requirement to send a new annual escrow statement.

154

TOPIC	ISSUE	RECOMMENDATION
16. Reasonable fees for nonpayment default, comment 35(b)(2)-2.iii	Comment 35(b)(2)-2.iii gives examples of fees for which a servicer lacks a reasonable basis to charge, including: "A default property management fee for borrowers that are not in a delinquency status that would justify the charge[.]" Some mortgage defaults are unrelated to late payments. Borrowers are required, for example, to maintain the property and are often required to repair it if it is damaged. Failure to do so as required is a default even if all payments are timely. For example, the GSE Uniform Security Instrument provides: "Lender may charge Borrower fees for services performed in connection with Borrower's default, for the purpose of protecting Lender's interest in the Property and rights under this Security Instrument, including, but not limited to, attorneys' fees, property inspection and valuation fees."	Servicers may charge borrowers appropriate fees to protect the servicer and investor from nonpayment defaults, even if the loan is current. The quoted comment should be amended to read: "A default property management fee for borrowers that are not in a ~~delinquency~~ **default** status that would justify the charge[.]"
17. Error under § 35(b)(7) should not include failure to provide complete loss mitigation information under § 39(b)(2),	Section 35(b)(7) defines error to include: "Failure to provide accurate information to a borrower regarding loss mitigation options and foreclosure, as required by § 1024.39." Section 39(b)(2) requires servicers to supply only "brief" loss mitigation information.	We request clarification that if a servicer has provided the information required by § 39(b)(2), *per se* there can be no error under § 35(b)(7). Specifically, the definition of error should not apply when a servicer provides all the information required by § 39(b)(2) even if it is not complete and exhaustive because § 39(b)(2)(iii) requires only a "brief description of examples of loss mitigation options that may be available from the servicer."
18. An error under § 35(b)(7) should include only duties that require information disclosure	Section 35(b)(7) defines error to include: "Failure to provide accurate information to a borrower regarding loss mitigation options and foreclosure, as required by § 1024.39."	We request clarification that the § 35(b)(7) definition of error includes only duties under § 39 that require disclosure of information.

TOPIC	ISSUE	RECOMMENDATION
	The referenced § 39 requires actions other than providing information; it requires attempting to contact a borrower.	
19. An error under § 35(b)(8) should not include failure to transfer useless information	Section 35(b)(8) defines error to include: "Failure to transfer accurately and timely information relating to the servicing of a borrower's mortgage loan account to a transferee servicer." Some information relates to "the servicing of a borrower's mortgage loan" that the transferee does not need. For example, the transferee normally does not need all communications between the transferor servicer and the investor for the period before the transferee is the servicer. Likewise, identification of which employee within the transferor servicer prepared a response to a QWR, or responded to a phone inquiry, likewise is not useful to the transferee servicer. There should be no requirement to transfer useless information. If there is a transfer of servicing but no change in the document custodian, not all the information will need to be transferred. In this case, there should be no requirement that the transferor or custodian transfer the custodian's files at all.	If the transferee and transferor servicers agree that particular information does or does not need to be transferred, failure to deliver the unnecessary should never be a violation. This way, the appropriate information will be transferred, but the regulation would not need to specify every conceivable piece of information that must be transferred in every scenario. We recommend revising § 35(b)(8) as follows: "Failure to transfer accurately and timely information relating to the servicing of a borrower's mortgage loan account **that the transferor and transferee agree should be transferred** to a transferee servicer."
20. Definition of "any other error," § 35(b)(11)	Section 35(b) defines error to include, in addition a list of errors: "Any other error relating to the servicing of a borrower's mortgage loan."	We request clarification that if the borrower does not specify an error, and the servicer cannot reasonably understand what error the borrower asserts, there is no error assertion.
21. Single intake address, § 35(c)	Section 35(c) permits servicers to designate an address for submissions of error assertions.	We request clarification that it is permissible to designate a single address for submissions of error assertions, information requests, and

TOPIC	ISSUE	RECOMMENDATION
		QWRs.
22. Change of intake address, 35(c)	Section 35(c) requires notice of a change in a designated intake address, but does not specify by when. Comment 38(b)(5)-1 provides that servicers may notify borrowers of the error assertion process by a notice (mailed or delivered electronically) or a website.	We suggest that if the new address is included on or with the last periodic statement delivered before the change becomes effective, that should be sufficient. If a servicer will designate the existing QWR address as the intake address for error assertions, no separate notice should be required when the regulation becomes effective.
23. Providing the designated address, comment 35(c)-2	Comment 35(c)-2 provides: "If a servicer establishes an address that a borrower must use to assert an error, a servicer must provide that address to the borrower in any communication in which the servicer provides the borrower with contact information for assistance from the servicer." This would be very broad, including even oral communications, and even if the borrower expressed an unwillingness to hear the information. It could be required on escrow statements, rate-reset notices, and IRS Forms 1098. It could also be required on initial and annual privacy notices even if the opt-out address is different that the error assertion address, possibly confusing borrowers. It would also require the intake address on force-placed insurance notices, which do not include this information and which prohibit additional information on the form. Sections 37(c)(4); (d)(4); and (e)(4). These provisions permit additional information on a separate piece of paper. However, including an intake address on a separate piece of paper would be wasteful, and would appear to indicate that the intake	We recommend that the address need be provided only: • Upon request; and • In periodic statements or coupon books.

157

TOPIC	ISSUE	RECOMMENDATION
	address is more important then the insurance information. Clearly the CFPB, therefore, did not intend that **all** communications include this intake address.	
24. Notice of right to request documents, § 35(e)(1)(i)(B)	Section 35(e)(1)(i)(B) requires responses to error assertions to state, among other things, how the borrower can request a copy of documents on which the servicer relied.	The servicer should be able to require such requests to be written so the servicer can be able to accurately determine whether a borrower made such a request.
25. Borrowers may or may not provide relevant information, § 35(e)(2)	An error resolution may require information that a borrower has and the servicer does not. The regulation does not permit the servicer to require the borrower to produce that information before investigating the asserted error, and does not permit the servicer to determine that no error occurred because the borrower failed to provide any requested information without conducting a reasonable investigation.	We request clarification that when a borrower does not provide requested, relevant information, and the servicer reasonably investigates the error assertion, the servicer's lack of that information should be a permissible basis to determine that no error occurred. If the servicer conducts a reasonable investigation and determines that the servicer needs information it does not possess, and determines that no error has occurred because the servicer lacks necessary information, that error notice should be deemed resolved. If the borrower thereafter supplies the missing information, that should be a new error notice subject to the full 5-day, 30-day, and 45-day response times. Otherwise, a borrower could wait until day 30 or day 45 to deliver the necessary information and the servicer would not have time for a reasonable investigation.
26. Time limits, § 35(e)(3)	Section 35(e)(3)(i)(B) requires servicers to respond to assertions of (b)(9) and (b)(10) errors by the earlier of 30 days from receipt or the date of the foreclosure sale. Comment 35(e)(3)(i)(B)-1 provides: "If a servicer cannot comply with its obligations pursuant to § 1024.35(e) by the earlier of a foreclosure sale or 30 days after receipt of the notice of error, a servicer may cancel or postpone a	The servicer should be held to a reasonableness standard. If the servicer cannot reasonably cancel or postpone a foreclosure sale, it should not be required to respond to the error assertion before the sale. It should be permissible to respond within 30 days and to take any appropriate remedial steps. Otherwise, borrowers would use this as a means to delay an appropriate

158

TOPIC	ISSUE	RECOMMENDATION
	foreclosure sale, in which case the servicer would meet the time limit in § 1024.35(e)(3)(i)(B) by complying with the requirements of § 1024.35(e) before the earlier of 30 days after receipt of the notice of error (excluding legal public holidays, Saturdays, and Sundays) or the date of the rescheduled foreclosure sale." The statement that servicers "may" cancel or postpone a foreclosure sale is not necessarily true. They will not be able to do so in all cases.	foreclosure. Borrowers would submit baseless error assertions at the last minute for the purpose of delaying foreclosures.
27. 15-day extension should be available long before a foreclosure sale, § 35(e)(3)	The general response time for error assertions is 30 days, extendable to 45 days upon notice to the borrower. The 15-day extension is not always available. Asserted (b)(9) and (b)(10) errors, which relate to foreclosures, require responses by the earlier of 30 days or the date of foreclosure, § 35(e)(3)(i)(C), without any extension, § 35(e)(3)(ii). If the foreclosure sale is scheduled for more than 45 days in the future, the servicer should be able to extend the response time.	The 15-day statutory extension should be available if the error assertion is received more than 45 days before a scheduled foreclosure sale.
28. Borrower requests for information on which servicer relied – multiple requests, § 35(e)(4)	Section 35(e)(4) requires servicers to provide upon request "copies of documents and information relied upon by the servicer in making its determination that no error occurred[.]" If a servicer provides all documents required to be provided, the request should be closed and responses to further requests for documents relied on should not be required.	After providing requested documents, the servicer should not be required to respond to requests for further documents on which it relied. We request clarification that if the servicer determines an error did occur and corrects it, providing documents relied on is unnecessary.
29. Borrower requests for information on which servicer relied – form should not matter, § 35(e)(4)	Sometimes the information a servicer relies on will be a screen shot of account activity. Servicers' systems are not always designed to provide printouts, and may not be in a form or format that is consumer-friendly. A screen shot of account activity, for example, will use "hieroglyphic" codes and terminology that the servicer understands but that a consumer does not.	There should be no need for costly systems changes to alter the form and not the substance of the information. It should be permissible for servicers to provide information in a form different from the form of the information when the servicer used it, and that conveys the same relevant information. There should not be an elevation of form over substance. For example, if a consumer alleges a payment was applied

159

TOPIC	ISSUE	RECOMMENDATION
		on the wrong date, the servicer should not be required to send a screen shot, but should be able to send a letter that says, "our records reflect that we received your payment due March 1, 2013 on March 16, 2013. We applied your payment as of March 16, 2013."
30. Attorney work product should not be subject to mandatory disclosure, § 35(e)(4)	Section 35(e)(4) does not require servicers to supply information that is confidential, proprietary, or privileged.	It should be clear that servicers are also not required to divulge information protected by the attorney work-product doctrine, even if that information is not privileged. These terms are not synonymous. *See* Federal Rule of Evidence 502.
31. General descriptions of materials withheld should be sufficient, § 35(e)(4)	Section 35(e)(4) provides: "If a servicer withholds documents relied upon because it has determined that such documents constitute confidential, proprietary or privileged information, the servicer must notify the borrower of its determination in writing within 15 days[.]"	It should be permissible for servicers to include a general description of materials withheld, to meet the 15-day deadline. It may not be reasonably possible to produce a privilege log that quickly, and one should not be required. A statement such as the following should be permissible: "We are not required to provide you with materials that are confidential, proprietary, privileged, or that are attorney work-product. We do not include any such information."
32. Frivolous or abusive error assertions should not require a response, § 35(g)	The error resolution process is not required when an error notice alleges a duplicative or overbroad error. That could mean it does apply to frivolous or abusive error assertions. For example, habitual late payers could send a baseless, but different, error assertion for each late payment to delay adverse, but accurate, credit reporting.	The error resolution procedure should not apply to frivolous or abusive error assertions.
33. Error assertions that are the subject of pending litigation should not require a response, § 35(g)		We recommend that servicers should not be required to respond to error assertions that are the subject of pending litigation because any response requirement would interfere with the discovery process overseen by neutral courts and the rules of procedure and evidence.
34. Error assertions buried	§ 35(g)(1)(ii) provides:	It is not clear how servicers are to reconcile these two provisions. We

TOPIC	ISSUE	RECOMMENDATION
in abusive error assertions, § 35(g)(1)(ii)	"To the extent a servicer can reasonably identify a valid assertion of an error in a notice of error that is otherwise overbroad, the servicer shall comply with the requirements of paragraphs (d), (e) and (i) of this section with respect to that asserted error." Comment 35(g)(1)(ii)-1.iii appears to contradict the regulation. It provides that an unduly burdensome error assertion includes: "Assertions of errors in a form that is not reasonably understandable or is included with voluminous tangential discussion or requests for information, such that a servicer cannot reasonably identify from the notice of error any error for which § 1024.35 requires a response."	recommend an additional example of an overbroad or unduly burdensome error assertion: "A submission that is unreasonably lengthy in relation to what it appears to assert."
35. Untimely error assertions, § 35(g)(1)(iii)(B)	The regulation does not require responses to error assertions submitted more than a year after the loan balance was paid in full. After a short sale, deed-in-lieu, or sale-leaseback, whether the loan is paid "in full" may not be clear, especially in states that do not permit deficiency judgments.	No response should be required more than a year after a servicer, assignee, or both, execute with a borrower or borrowers a short sale, deed-in-lieu of foreclosure, sale-leaseback, or similar nonretention foreclosure alternative.
36. Notice to borrower that servicer is not required to respond to error assertion, §35(g)(2)	Section 35(g)(2) provides: "If a servicer determines that, pursuant to this paragraph (g), the servicer is not required to comply with the requirements of paragraphs (d), (e) and (i) of this section, the servicer shall notify the borrower of its determination in writing not later than five days (excluding legal public holidays, Saturdays, and Sundays) after making such a determination. The notice to the borrower shall set forth the basis under paragraph (g)(1) of this section upon which the servicer has made such determination."	Servicers that receive duplicative, overbroad, untimely, abusive, or frivolous error assertions should not be required to repeatedly send the § 35(g)(2) notice that no response is required. Congress directed the CFPB to put an end to abusive QWRs. RESPA § 6(k)(1)(B). There is no reason servicers should remain required to respond to abusive notices or inquiries. We recommend that a servicer be required to send no more than two § 35(g)(2) notices in response to similar error assertions in connection with the same loan.

161

TOPIC	ISSUE	RECOMMENDATION
	Borrowers can repeatedly send the servicer the same notice of error over and over again, and the servicer would have to send the non-responsive response each time. This is unduly burdensome on the servicer and offers no consumer benefit.	
37. Limits on adverse credit reporting, § 35(i)	Section 35(i) provides: "After receipt of a notice of error, a servicer may not, for 60 days, furnish adverse information to any consumer reporting agency regarding any payment that is the subject of the notice of error."	To prevent borrower abuse, this prohibition should not apply after a servicer determines that a response is not required. Otherwise, habitual late payers could send a baseless, but different, error assertion for each late payment to delay adverse, but accurate, credit reporting.
Information Requests, § 36		
38. Scope of requests that require responses, § 36(a) and 36(f)(1)(iii)	The § 35 definition of error is limited to servicing-related errors. There is no analogous definition of information request. A QWR that requests information "relating to servicing the mortgage loan" is an information request, but non-QWR information requests do not need to relate to servicing. Section 36(f)(1)(iii) says servicers do not need to respond to requests for information that is not directly related to the borrower's mortgage loan account. However, this is not limited to servicing information. It apparently requires servicers to provide any requested origination information. The CFPB states in its section-by-section analysis: "[T]he Bureau does not believe that the information request procedures should replace or supplant civil litigation document requests and should not be used as a forum for pre-litigation discovery."	Including origination information in the scope of the information request procedures would create a "back-door" discovery process, especially in light of both the ability-to-repay rule and the Administration's approach to disparate impact liability. We agree with the CFPB that discovery should be overseen by an impartial judge who can weigh the importance of the information against the costs of producing it. <u>Ability-to-Repay "Back Door" Discovery</u> Consumers will have an incentive to establish that a purported QM loan was not a QM loan, and will use this servicing rule for pre-litigation fishing expeditions. As this was not the CFPB's intent, we recommend adding additional examples of irrelevant information to comment 36(f)(1)(iii), including: • Information that relates to whether the loan was originated in

TOPIC	ISSUE	RECOMMENDATION
	78 Fed. Reg. 10696, 10761 (Feb. 14, 2013).	compliance with the ability-to-repay rule, 12 C.F.R. § 1026.43; • Information that relates to the whether points and fees on the loan, as defined in 12 C.F.R. § 1026.32(b), exceeded a threshold under the QM definition, the HOEPA definition, a similar definition under state law, or under § 941 of the Dodd-Frank Act (risk retention). <u>Disparate Impact "Back-Door" Discovery</u> Borrowers have a strong incentive to show that a loan was originated, serviced, or treated in the secondary market, with a "disparate impact" on a class, or on classes, of borrowers. Such allegations can lead to large settlements without actual showing of impropriety, thereby providing a strong incentive to use this servicing rule for pre-litigation fishing expeditions. As this was not the CFPB's intent, we suggest additional examples in the same comment, including: • Information that relates to any loan other than the borrower's loan that is serviced by the servicer to whom the information request is made; • Information that relates to any loan application or loan applicant other than the borrower's application and the borrower; • Information that relates to any borrower or loan applicant other than the borrower who made, or on whose behalf was made, the information request; • Information that relates to the practices of the servicer or the originating lender in connection with loans, loan applications, and loan defaults generally, including the borrower's loan and other loans, borrowers, or applicants. <u>Risk Retention is Irrelevant to Consumers</u>

TOPIC	ISSUE	RECOMMENDATION
		Comment 36(f)(1)(ii)-1.i treats as confidential, proprietary or privileged information regarding the servicer's profitability and information provided to investors. Risk retention information does not affect the borrower's obligations, the borrower's loan payments, or any aspects of the borrower's experience with the loan, so servicers should not be required to produce this information outside of actual discovery overseen by an impartial judge. We suggest adding to the examples: "Information that relates to any risk retention or other requirement that may arise in connection with the loan or its securitization, under Dodd-Frank § 941."
39. Single intake address, § 36(b)	Section 36(b) permits servicers to designate an address for submissions of information requests.	We request clarification that it is permissible to designate a single address for submissions of error assertions, information requests, and QWRs.
40. Change of intake address, 36(b)	Section 36(b) requires notice of a change in a designated intake address, but does not specify by when. Comment 38(b)(5)-1 provides that servicers may notify borrowers of the information request process by a notice (mailed or delivered electronically) or a website.	We suggest that if the new address is included on or with the last periodic statement delivered before the change becomes effective, that should be sufficient. If a servicer will designate the existing QWR address as the intake address for information requests, no separate notice should be required when this rule becomes effective.
41. Providing the designated address, comment 36(b)-2	Comment 36(b)-2 provides: "If a servicer establishes an address that a borrower must use to request information, a servicer must provide that address to the borrower in any communication in which the servicer provides the borrower with contact information for assistance from the servicer."	This would be very broad, including even oral communications. We recommend that the address need be provided only: • Upon request; and • In periodic statements or coupon books.

TOPIC	ISSUE	RECOMMENDATION
	This would be overbroad, as discussed under comment 35(c)-2 above.	
42. Format of information provided should be irrelevant, § 36(d)(1)	Section 36(d)(1) requires servicers to provide available requested information. Some requested information will be available in the form of a screen shot of account activity. The systems that produce the screen shots are not always designed to provide printouts, and may not be in a form or format that is consumer-friendly. A screen shot of account activity, for example, will use "hieroglyphic" codes and terminology that the servicer understands but that a consumer does not.	There should be no need for costly systems changes to alter the form and not the substance of the information. It should be permissible for servicers to provide information in a form different from the form in which the servicer stores the information, and that conveys the same relevant information. There should not be an elevation of form over substance. For example, if a consumer asks when a payment was applied, the servicer should not be required to send a screen shot, but should be able to send a letter that says, "our records reflect that we received your payment due March 1, 2013 on March 16, 2013. We applied your payment as of March 16, 2013."
43. Reasonableness standard of information availability does not consider all relevant information; additional examples needed, comment 36(d)(1)(ii)	Comment 36(d)(1)(ii) provides examples of when information is or is not available, using the terms "ordinary course of business," "extraordinary efforts," and "reasonable efforts." These are subjective standards, so it is not clear what compliance requires. For example, comment 36(d)(1)(ii)-2.iii gives an example of information being available "through reasonable efforts in the ordinary course of business" when the servicer has a legal right to access the information and the actual ability to find it. This does not consider the cost of traveling to the facility and making the search. The examples seem to consider whether it is physically possible to retrieve the information before the deadline, which is appropriate. However, none of the examples considers the cost to the servicer, and none weigh that cost against the usefulness of the information to the borrower for an appropriate purpose.	A reasonableness standard should apply to § 36(d)(1) as well as to § 36(f)(1)(iv). A reasonableness standard needs to weigh both: • The servicer's actual costs, in both time and money; • The usefulness of the information to the borrower in understanding the terms of the loan and security instrument, or in performing on the loan. A reasonableness standard should not take into account the usefulness of the information to the borrower for "back-door" discovery or other inappropriate purposes. We urge additional, much more specific, examples, such as: • If a servicer stores requested information offsite, or in a form that is likely not accessible to the borrower, then whether the information is available depends on whether the servicer can retrieve the information, in a format likely accessible to the borrower, within the

165

TOPIC	ISSUE	RECOMMENDATION
	Section 36(f)(1)(iv) does not require a response to information requests that are unduly burdensome, using a reasonableness standard: "An information request is unduly burdensome if a diligent servicer could not respond to the information request without either exceeding the maximum time limit permitted by paragraph (d)(2) of this section or incurring costs (or dedicating resources) that would be unreasonable in light of the circumstances."	time limits in § 36(d)(2), at a cost that is reasonable, in relation to the apparent usefulness of the information to the borrower's understanding of the terms of the loan and security instrument or the borrower's performance on the loan. • If a servicer stores requested information offsite, and in the ordinary course of business goes to the off-site storage facility once per calendar month, the information is available only if the servicer can obtain the information in a regular trip to the offsite facility in time to retrieve the information and deliver it in accordance with § 36(d) within the time limit in § 36(d)(2). • If a servicer stores requested information in a location where there was an accident, disaster, power failure, snowstorm, or similar event that makes delivering the information within the § 36(d)(2) deadline unreasonably difficult, the information is unavailable.
44. Format of information provided, comments 36(d)(1)(ii)-2.i and 36(f)(1)(iv)-1.iii	Comment 36(d)(1)(ii)-2.i provides that information is available when: "The servicer's personnel have access in the ordinary course of business to audio recording files with organized recordings or transcripts of borrower telephone calls and can identify the communication referred to by the borrower through reasonable business efforts." Comment 36(f)(1)(iv)-1.iii provides that information need not be delivered: "[I]n specific formats, such as in a transcript, letter form in a columnar format, or spreadsheet, when such information is not ordinarily stored in such format[.]"	If a servicer has available a recording of a relevant call but not a transcript of it, the servicer is not required to transcribe the call to comply with the information request requirements. If the format of the recording is not compatible with consumer devices, must the servicer deliver something the consumer cannot use?

TOPIC	ISSUE	RECOMMENDATION
45. Frivolous or abusive information requests should not require a response, § 36(f)(1)	Section 36(f)(1) provides that servicers are not required to respond to information requests that are duplicative, overbroad, or unduly burdensome. This could mean a response is required to frivolous or abusive information requests. Comment 36(f)(1)(iv)-1 provides examples of overbroad or unduly burdensome requests that are similar to abusive QWRs under current law. This is appropriate. However, we are concerned that when those abusive requests no longer require responses, the abusive requests will change form just enough to fall outside the examples in this comment. For example, instead of sending one overbroad request, new requests may take the form of a large number of narrow, but not overlapping, requests. This would defeat the purpose of preventing abusive requests.	Frivolous or abusive requests should not require a response. Examples in a regulation or commentary would be helpful. We suggest the following examples: • Apparent back-door discovery requests, even if not, individually, overbroad or unduly burdensome. For this purpose, multiple information requests regarding the same loan may be considered together even if submitted separately or at different times. • Requests about underwriting standards that the loan originator used or did not use. • Requests for information about how a lender, settlement agent, or mortgage broker set or sets loan terms or loan charges. • Requests for information about how a servicer set or sets its servicing or default charges. • Requests for information about how a service provider set or sets its charges. • Requests about any risk retention requirements that may be applicable to the loan. • Requests about a different loan, even if the servicer is the same servicer.
46. Requests for information that are the subject of pending litigation should not require a response, § 36(f)		We recommend that servicers should not be required to respond to requests for information that are the subject of pending litigation because any response requirement would interfere with the discovery process overseen by neutral courts and the rules of procedure and evidence.
47. Attorney work product should not be subject to mandatory disclosure,	Section 36(f)(1)(ii) does not require servicers to supply information that is confidential, proprietary, or privileged.	It should be clear that servicers are also not required to divulge information protected by the attorney work-product doctrine, even if that information is not privileged. These terms are not synonymous.

167

TOPIC	ISSUE	RECOMMENDATION
§ 36(f)(1)(ii)		*See* Federal Rule of Evidence 502.
48. Information requests buried in abusive information requests, § 36(f)(1)(iv)	Section 36(f)(1)(iv) provides: "To the extent a servicer can reasonably identify a valid information request in a submission that is otherwise overbroad or unduly burdensome, the servicer shall comply with the requirements of paragraphs (c) and (d) of this section with respect to that requested information." Comment 36(f)(1)(iv)-1.ii appears to contradict the regulation. It provides that an unduly burdensome request includes: "Requests for information that are not reasonably understandable or are included with voluminous tangential discussion or assertions of errors[.]"	It is not clear how servicers are to reconcile these two provisions. We recommend an additional example of overbroad or unduly burdensome information requests: "A submission that is unreasonably lengthy in relation to what it appears to request."
49. Untimely requests, § 36(f)(1)(v)	Section 36(f)(1)(v) does not require responses to information requests submitted more than a year after the loan balance was paid in full. After a short sale, deed-in-lieu, or sale-leaseback, whether the loan is paid "in full" may not be clear, especially in states that do not permit deficiency judgments.	No response should be required more than a year after a servicer, assignee, or both, execute with a borrower or borrowers a short sale, deed-in-lieu of foreclosure, sale-leaseback, or similar nonretention foreclosure alternative.
50. Notice to borrower that servicer is not required to respond to information request, § 36(f)(2)	Section 36(f)(2) provides: "If a servicer determines that, pursuant to this paragraph (f), the servicer is not required to comply with the requirements of paragraphs (c) and (d) of this section, the servicer shall notify the borrower of its determination in writing not later than five days (excluding legal public holidays, Saturdays, and Sundays) after making such a determination. The notice to the borrower shall set	Servicers that receive duplicative, overbroad, untimely, abusive, or frivolous information requests should not be required to repeatedly send the § 36(f)(2) notice that no response is required. Congress directed the CFPB to put an end to abusive QWRs. RESPA § 6(k)(1)(B). There is no reason servicers should remain required to respond to abusive notices or inquiries.

TOPIC	ISSUE	RECOMMENDATION
	forth the basis under paragraph (f)(1) of this section upon which the servicer has made such determination." Borrowers can repeatedly send the servicer the same request for information over and over again, and the servicer would have to send the non-response notice each time. This is unduly burdensome on the servicer and offers no consumer benefit.	We recommend that a servicer be required to send no more than two § 36(f)(2) notices in response to similar information requests in connection with the same loan.
51. General descriptions of materials withheld should be sufficient, § 36(f)(2)	If a servicer determines that it is not required to deliver requested information, it must notify the borrower within only five days: "The notice to the borrower shall set forth the basis under paragraph (f)(1) of this section upon which the servicer has made such determination."	It should be permissible for servicers to include a general description of materials withheld, to meet the 5-day deadline. It would usually not be possible to produce a privilege log in only five days, and one should not be required. A statement such as the following should be permissible: "We are not required to provide you with materials that are confidential, proprietary, privileged, or that are attorney work-product. We do not include any such information."
Force-Placed Insurance, § 37		
52. Servicers need to be able to require sufficient insurance coverage, § 37	There have been court cases questioning whether servicers can require required insurance. *See:* Kolbe v. BAC Home Loans Servicing, 695 F.3d 111 (1st Cir. 2012), reversing dismissal of claims that requiring flood insurance coverage equal to the replacement cost, and above the amount required by the NFIA, because the claims state a plausible breach of contract. Lass v. Bank of America, 695 F.3d 129 (1st Cir. 2012), reversing dismissal of claims, holding that lender did not have discretion to	We request that the CFPB make very clear that: • A servicer that complies with § 37 has the right to require insurance coverage in an amount, and of a type, that the servicer determines is permitted or required by the security instrument, investor guidelines, safety and soundness standards, or that is required by law. • The servicer may require more flood insurance coverage than the NFIA requires, such as to cover the replacement cost of the property. This is an important protection that can prevent consumers from losing their homes, as well as a safety and soundness requirement.

TOPIC	ISSUE	RECOMMENDATION
	modify the flood insurance requirement during the life of the loan. _Ellsworth v. U.S. Bank_, 12-0256 (N.D. Ca. 2012), denying lender's motion to dismiss a putative class action because the mortgage can be read to restrict lender's discretion in force-placing flood insurance. _Casey v. Citibank, et. al._ 5:12-cv-820 (N.D.N.Y. 2013), denying motion to dismiss claims that mortgages did not permit servicer to increase the amount of required flood insurance coverage. _Arnett v. Bank of America_, 874 F. Supp.2d 1021 (D. Or. 2012), denying defendant's motion for judgment on the pleadings in putative class action because the mortgage does not give the mortgagee the right to set the amount of flood insurance required. This type of litigation should be unnecessary. Consumers can be seriously harmed by insufficient insurance coverage. For that very reason, servicers have a right to require insurance coverage in an amount, and of a type, that is permitted or required by the security instrument, investor guidelines, safety and soundness standards, or that is required by law.	• The amount of required insurance coverage may increase during the life of the loan. • A property that was not in a special flood hazard area ("SFHA") at origination may, in the future, be designated as in an SFHA, in which case the servicer should be able to require an appropriate amount of flood insurance coverage.
53. Servicers need to require flood insurance when not required by the FDPA, § 37(a)	Section 37(a) provides: "For the purposes of this section, the term 'force-placed insurance' means hazard insurance obtained by a servicer on behalf of the owner or assignee of a mortgage loan that insures the property securing such loan." The definition does not include flood insurance required by the FDPA.	Servicers should be able to require insurance coverage even when not mandated by applicable law or when not available under the FDPA. This is both a consumer protection and a safety and soundness protection. The CFPB should state in a comment that the statement in the Model Form MS-3(D) that insurance "is required" can mean is required by the servicer even if it is not required by applicable law, or was required

TOPIC	ISSUE	RECOMMENDATION
	Section 37(a)(2)(i). Servicers sometimes require flood insurance: • On properties in an SFHA but not in a participating community, so the FDPA does not apply and does not require insurance. • On properties in an SFHA but in a Coastal Barrier Resource Act ("CBRA") and Otherwise Protected Areas ("OPA") zones, where the FDPA does not apply and does not require insurance. • On a property that was designated as in an SFHA at origination, and later designated as out of an SFHA. • On a property that is in certain areas not in an SFHA, such as a Mississippi Grant Program. The Model Notices appear only to apply to instances where insurance "is required." Required by whom or what is unclear.	when making, increasing, extending, or renewing a loan, even if the property is no longer in a SFHA (*see* the next item).
54. Definition of force-placed insurance and properties remapped out of a SFHA, § 37(a)(2)	Section 37(a)(2) defines force-placed insurance to exclude insurance required by the FDPA. What is the status of flood insurance retained on a property that is remapped out of a SFHA (or on a property that is in a CBRA, OPA, or non-participating community)? If a servicer requires flood insurance on a property for the life of the loan, even if the property is remapped out of a SFHA after origination, such insurance should not be considered force-placed insurance unless the servicer is required to force-place an NFIP MPPP policy or force-place a private flood insurance policy. Continued maintenance of a borrower-purchased flood insurance policy obtained as a condition of origination is not force-placement. This is consistent with § 1024.17 which distinguishes force-placed insurance from situations in which a servicer renews borrowers' own hazard insurance policies. We seek clarity of this fact. It appears that the regulation permits renewal of	In all cases, we believe that obtaining or renewing a borrower-purchased flood insurance policy even if not mandated by the FDPA is not force-placed insurance and does not trigger § 37. Otherwise stated, servicers that continue to escrow and pay for borrower-purchased flood insurance on a property that was located in a SFHA at origination but is later remapped out of a SFHA should not be considered to be force-placing insurance. Because servicers are not required to track the continuing SFHA status of a property by law, servicers can and sometimes do require flood insurance for the life of the loan even if not mandated by FDPA to do so.

TOPIC	ISSUE	RECOMMENDATION
	flood insurance only if the property remains designated as in an SFHA or the borrower consents. Requiring servicers to track SFHAs after a mortgage loan is originated is inconsistent with the FDPA and its implementing regulations. We note that the laws governing flood insurance are not federal consumer financial laws within the CFPB's authority. Congress expressly directed prudential regulators to require lenders to look at SFHA status at origination but not throughout the life of the loan: "[B]y regulation direct regulated lending institutions— (A) not to **make, increase, extend, or renew any loan** secured by improved real estate or a mobile home located or to be located in an area that has been identified by the Administrator as an area having special flood hazards and in which flood insurance has been made available under the National Flood Insurance Act of 1968 [42 U.S.C. 4001 et seq.], unless the building or mobile home and any personal property securing such loan is covered for the term of the loan by flood insurance in an amount at least equal to the outstanding principal balance of the loan or the maximum limit of coverage made available under the Act with respect to the particular type of property, whichever is less[.]" 42 U.S.C. § 4012a(b)(1) (emphasis added). Required insurance premiums must be escrowed in certain circumstances, 42 U.S.C. § 4012a(d), but "[t]his subsection shall apply only with respect to any loan **made, increased, extended, or renewed** after the expiration of the 1-year period beginning on September 23, 1994." *Id.* at (d)(5) (emphasis added). This does not require servicers to track whether a	

172

TOPIC	ISSUE	RECOMMENDATION
	property that was in a SFHA at origination remains in one. The prudential regulators considered, but rejected, requiring servicers to track whether properties remain designated as in SFHAs: "Proposed question and answer 2 explained that, upon a FEMA map change that results in a building or mobile home securing a loan being removed from an SFHA, a lender is no longer obligated to require mandatory flood insurance. The Agencies received one comment from an industry group suggesting the guidance in proposed question and answer 2 be amended to add language encouraging lenders to promptly remove the flood insurance requirement from a loan when the building or mobile home securing the loan is removed from an SFHA by way of a map change. The decision to require flood insurance in these instances is typically made on a case-by-case basis, depending on a lender's risk management practices. The Agencies do not believe that a blanket statement encouraging lenders to remove flood insurance in such instances is an appropriate position; therefore, the question and answer is adopted as proposed." 74 Fed. Reg. 35914, 35916 (July 21, 2012). And: "The agencies reiterate their view that the Reform Act does not require lenders to engage in retroactive or prospective portfolio reviews or any other specific method for carrying out their responsibilities under the Federal flood insurance statutes. The Reform Act clearly requires lenders to check the status of security property for loans when triggered by the statutory tripwires. The Reform Act did not add remappings to the list of statutory tripwires.	

TOPIC	ISSUE	RECOMMENDATION
	The Reform Act does not require lenders to monitor for map changes, and the agencies will not impose such a requirement by regulation." 61 Fed. Reg. 45684, 45693 (August 29, 1996). The prudential regulators do not have authority to require life-of-loan map tracking. The prudential regulators are, but not the CFPB is not, authorized to implement flood insurance laws. The CFPB does not have authority to require life-of-loan map tracking that Congress and the prudential regulators have explicitly rejected.	
55. Insurance as a condition of a loan when voluntary coverage is unavailable, § 37(a)(2)	When voluntary insurance coverage is unavailable, lenders may require the borrower to enter into the lender's force-placed insurance program as a condition of making the loan.	We recommend that in these cases, the insurance not be defined as force-placed under § 37(a)(2).
56. Reasonable response time, § 37(c) and (g)	Section 37(c) requires servicers to notify borrowers before force-placing insurance. Section 37(g) requires servicers to refund premiums for duplicative force-placed insurance if the borrower demonstrates sufficient insurance coverage, but apparently without any requirement that the borrower act in a reasonable amount of time.	We recommend that servicers be permitted to require borrowers who have sufficient insurance coverage to demonstrate that coverage to the servicer within a reasonable amount of time, such as 60 days from the first date of coverage, as a prerequisite to applicability of § 37(g).
57. Evidence demonstrating insurance, comment 37(c)(1)(iii)-2	Comment 37(c)(1)(iii)-2 makes clear that a servicer may require a declaration page or other similar information, and may reject evidence of insurance that does not "provide[ ] confirmation" of the information. This is quite helpful. The same standard should apply uniformly, including under §§ 37(d)(2)(ii), (e)(1)(ii), and (g). There is a cross-reference to this comment in comment 37(e)(1)-1, which is also quite helpful. There is	We recommend cross-referencing comment 37(c)(1)(iii)-2 in comments under §§ 37(d)(2)(ii) and (g), to make clear that the same standard applies under those provisions as well.

TOPIC	ISSUE	RECOMMENDATION
	no cross-reference in comments under §§ 37(d)(2)(ii) or (g). The standard under these provisions, absent a comment, would be "evidence demonstrating" insurance coverage. Evidence may be substantially less reliable or accurate than a declaration page, and may not be a confirmation at all.	
58. Additional information in a disclosure, § 37(c)(4), (d)(4), (e)(4)	The regulation prohibits including additional information on the insurance notices. Some additional information may be appropriate.	We request model language for disclosures as follows: • A statement providing the borrower with the correct mortgagee clause; this ensures the documentation for next year's renewal makes it to the right place, potentially avoiding the need for notification again next year. This is both a consumer convenience and a courtesy. • For bankruptcy cases, language that this disclosure is not an attempt to collect a debt. The section-by-section analysis in Regulation Z contains this language: "For example, servicers may include a statement such as: 'To the extent your original obligation was discharged, or is subject to an automatic stay of bankruptcy under Title 11 of the United States Code, this statement is for compliance and/or informational purposes only and does not constitute an attempt to collect a debt or to impose personal liability for such obligation. However, Creditor retains rights under its security instrument, including the right to foreclose its lien.'" 78 Fed. Reg. 10902, 10966 (February 14, 2013). We request incorporation of this language into the commentary so that its use would be protected. • A statement alerting the borrower that the servicer will offer or

TOPIC	ISSUE	RECOMMENDATION
		establish an escrow account for payment of the insurance premiums. • A statement that the insurance may not protect the consumer's interest in the property. We also request clarification that it is permissible to include the loan number on the disclosures. This is important for borrowers who have more than one property, and it is important for servicers' need to manage their records.
59. Additional pages, § 37(c)(4), (d)(4), (e)(4)	The regulation requires notices to be separate: "A servicer may not include any information other than information required by [specified] paragraphs [varies] in the written notice required by [specified] paragraph [varies]. However, a servicer may provide such additional information to a borrower on separate pieces of paper in the same transmittal."	It should be permissible to include additional information on the second side of one piece of paper. This would be consistent with comments 39(b)(2)-1 and -2, which permit servicers to combine 45-day delinquency notices with other information as long as all statements meet the clear and conspicuous standard of § 32(a)(1).
60. Estimated premiums, § 37(d)(2)(i)(D), (e)(2)(viii)(C)	Notices under § 37(d)(2) and (e)(2) require an estimate of insurance premiums when the servicer does not know the exact cost. It is unclear how servicers will be required to estimate premiums. Comment 37(e)(2)(i)(D)-1 states that the estimates must be based on information "reasonably available" to the servicer when the disclosure is provided, but it is not clear what type of information servicers must or may use. The comment also states that an estimate based on the borrower's delinquency status is permissible, but does not state whether servicers must consider delinquency status in all cases. The model forms note that the premium may be estimated, but draw very little attention to the word "estimated."	• The fact that an estimated premium amount turns out to be incorrect should *per se* not be a violation of § 37, a UDAP, or a UDAAP. • We suggest examples of how servicers will be permitted to estimate premiums, such as: o Give a range of dollar amounts; o Use the average premium of force-placed insurance at any point in the past twelve months on a sample of loans, regardless of how the sample is selected; o Use 150 percent of the cost of the most recent voluntary insurance policy on the property. • Servicers should be permitted to draw attention to the fact that a premium amount is estimated, such as on the back of the page or on a separate piece of paper. Statements that the estimate is not from

TOPIC	ISSUE	RECOMMENDATION
		an insurer, is not based on the same information an insurer would use, and that the actual cost may be much different than the estimate, all should be permitted.
61. Renewal of policies that predate January 10, 2014, § 37(e)	There will be some force-placed policies in effect on January 10, 2014. How the new regulation will apply to them is not clear.	We request clarification that a policy that was effective on January 10, 2014 that is renewed is subject to the renewal requirements in § 37(e), but does not need to go through the 45-day notice process for new policies.
62. Annual renewal notices, § 37(e)(5)	Section 37(e)(5) requires annual renewal notices, but does not define "year" as a calendar year or 365 days. It provides: "A servicer is not required to provide the written notice required by paragraph (e)(1) of this section more than once a year."	We request clarification that a servicer may send a renewal notice before the policy expires, and renew the policy on the expiration date. We also request clarification of annual notice timing. If a servicer sends a notice on June 1 in year 1, is the next notice due by the next June 1, or by December 31, in year 2? Operationally, it may be easier to send the notices at the same time in each calendar year. This should be permissible. This would be consistent with annual notices under Regulation P (consumer financial privacy) § 1016.5, which provides this reasonable flexibility: "(a)(1) *General rule.* You must provide a clear and conspicuous notice to customers that accurately reflects your privacy policies and practices not less than annually during the continuation of the customer relationship. *Annually* means at least once in any period of 12 consecutive months during which that relationship exists. You may define the 12-consecutive-month period, but you must apply it to the customer on a consistent basis. (2) *Example.* You provide a notice annually if you define the 12-consecutive-month period as a calendar year and provide the annual notice to the customer once in each calendar year following the

177

TOPIC	ISSUE	RECOMMENDATION
		calendar year in which you provided the initial notice. For example, if a customer opens an account on any day of year 1, you must provide an annual notice to that customer by December 31 of year 2."
63. Refunds, § 37(g)(2)	Section 37(g)(2) requires that , after cancelling a policy, servicers must: "Refund to such borrower all force-placed insurance premium charges and related fees paid by such borrower for any period of overlapping insurance coverage and remove from the borrower's account all force-placed insurance charges and related fees for such period that the servicer has assessed to the borrower."	We request clarification that the servicer may either make a direct refund or place it in the borrower's escrow account.
64. *Bona fide* and reasonable charge, § 37(h)(2)	Section 37(h)(2) requires charges for force-placed insurance to be *bona fide* and reasonable, defined as: "[A] charge for a service actually performed that bears a reasonable relationship to the servicer's cost of providing the service, and is not otherwise prohibited by applicable law."	We request clarification that the charge can include the cost of premiums, as well as the servicer's cost of administering its force-placed insurance.
Servicing Policies and Procedures, § 38		
65. Compliance standard under § 38(a)	Section 38(a) requires servicers to "maintain policies and procedures that are reasonably designed to achieve" a list of objectives. The CFPB explains: "This revision [from the proposed rule] will also allow the Bureau to protect borrowers through robust supervision and enforcement of the servicing policies, procedures, and requirements set forth in § 1024.38 without having to demonstrate a pattern or practice of violations."	We request clarification that: • The failure to achieve an objective is not itself a violation of the regulation; • The servicer's selection of "reasonably designed" policies and procedures does not require the most conservative or most strict possible policies and procedures, or the most advanced technology available; and • The factors affecting the reasonableness of the policies and

178

TOPIC	ISSUE	RECOMMENDATION
	The compliance standard is not clear.	procedures include: ○ The costs and resources involved in implementing, revising, and maintaining the policies and procedures; and ○ The servicer's need, and its affiliates' needs, to allocate resources to come into compliance with other rules, such as other Dodd-Frank rules.
66. Consumer complaints, comment 38(a)-1	Comment 38(a)-1 provides that servicers must base their policies, procedures, and requirements on, among other things, the servicer's history of consumer complaints. Not all complaints are valid or accurate, and some do not relate to servicing matters at all.	Servicers should not be required to base their policies, procedures, and requirements on baseless, unfounded, or irrelevant complaints.
67. Delegating corrections to service providers, comment 38(b)(1)(ii)-1	Comment 38(b)(1)(ii)-1 provides: "*Errors committed by service providers.* A servicer's policies and procedures must be reasonably designed to provide for promptly obtaining information from service providers to facilitate achieving the objective of correcting errors resulting from actions of service providers, including obligations arising pursuant to § 1024.35." Servicers should have the flexibility to delegate to service providers the task of correcting a service provider's errors. The comment appears to require the servicer to correct such errors directly, even if this is not the most effective method. It also assumes that information must come from a service provider, when notice of an error may come from, for example, the borrower. The source of the information is irrelevant.	The servicer, the service provider who made the error, or another service provider, should be permitted to make a correction. The source of the information used in a correction should not be relevant. We recommend amending the language as follows: "*Errors committed by service providers.* A servicer's policies and procedures must be reasonably designed to provide for **the servicer or a service provider to** promptly obtain~~ing~~ information ~~from service providers~~ to facilitate achieving the objective of correcting errors resulting from actions of service providers, including obligations arising pursuant to § 1024.35."
68. Providing information "with respect to" the mortgage loan, § 38(b)(1)(iii)	An objective under § 38(b)(1)(iii) is to: "Provide a borrower with accurate and timely information and documents in response to the borrower's requests for information	This objective should not create a "back-door discovery" avenue. We suggest that it be limited to "**reasonable** requests for information with respect to **servicing** the borrower's mortgage loan."

TOPIC	ISSUE	RECOMMENDATION
	with respect to the borrower's mortgage loan[.]" This includes matters that are well beyond the scope of a servicer's role, and could reach confidential, proprietary, privileged information or attorney work product. *See* the comments above under Scope of requests that require responses, § 36(a) and 36(f)(1)(iii).	
69. Information to investors about "all mortgage loans they own," § 38(b)(1)(iv)	An objective under § 38(b)(iv) is to: "Provide owners or assignees of mortgage loans with accurate and current information and documents about all mortgage loans they own[.]" This would include loans the investor owns that another servicer services, and would include commercial loans.	It should be limited to "all **consumer** mortgage loans they own **that the servicer services.**"
70. Identifying the successor in interest, § 38(b)(1)(vi)	An objective under § 38(b)(vi) is to: "Upon notification of the death of a borrower, promptly identify and facilitate communication with the successor in interest of the deceased borrower . . . ." It is not necessarily possible to identify the successor in interest "promptly." The borrower's family may not know, and may not agree. Some estates are litigated for years over this question. We are uncertain what problem the CFPB is trying to address with this objective. The family of a deceased borrower typically tries to avoid losing the property. Often, the family simply continues making payments without notifying the servicer of the borrower's death.	We recommend removing this objective. At a minimum, it should be revised to read: "Upon notification of the death of a borrower and of the borrower's successor in interest, promptly facilitate communication with the successor in interest . . . ."

TOPIC	ISSUE	RECOMMENDATION
	Servicers answer questions and continue to send periodic statements and other disclosures. It is not clear what additional information the CFPB intends for the servicer to communicate to the family.	
71. Transferring information in a servicing transfer, § 38(b)(4)	Section 38(b)(4) provides that the servicing policies and procedures must be reasonably designed to ensure that the servicer can: "As a transferor servicer, timely transfer **all** information and documents in the possession or control of the servicer relating to a transferred mortgage loan to a transferee . . . ." This should not require a transferor servicer to deliver "all" information, including all copies of documents. The transferor, under § 35, will be required to respond to information requests for a year after the servicing transfer, so the transferor will need to retain sufficient information to do so. Section 38(c)(1) requires transferor servicers to retain records for a year after a transfer. If there is a transfer of servicing but no change in the document custodian, not all the information will need to be transferred. In this case, there should be no requirement that the transferor or custodian transfer the custodian's files at all.	The transferor and transferee should be able to agree on what information is required to be to transferred. This is consistent with § 38(b)(4)(ii), which seems to contemplate that the transferee will have the contractual right to receive the information it needs. If the transferor delivers all the information the agreement requires, there should be no need to transfer additional information. There is no reason to restrict information the transferor may retain.
72. Privileged or protected information in a servicing transfer, comment 38(b)(4)(i)-2	Comment 38(b)(4)(i)-2 requires: "A transferor servicer's policies and procedures must be reasonably designed to ensure that the transfer includes . . . any analysis by a servicer with respect to potential recovery from a nonperforming mortgage loan, as appropriate."	There should be an exception to this comment that permits transferors to decline to transfer information that is privileged or otherwise protected from disclosure under any applicable law or investor requirement.

TOPIC	ISSUE	RECOMMENDATION
	It is possible that some of this information will be privileged or protected. Servicers do not own records related to Fannie Mae or Freddie Mac loans and may not have authority to transfer protected materials. For example, some information may be protected by the attorney-client privilege, and the privileged information is the GSE's property. The servicer should not be required to waive a GSE's privilege. Fannie Mae's Servicing Guide at § 401 provides: "All records pertaining to mortgage loans sold to Fannie Mae—including but not limited to the following—are at all times the property of Fannie Mae and any other owner of a participation interest in the mortgage loan: [lengthy list omitted.] . . . These documents and records are Fannie Mae's property regardless of their physical form or characteristics or whether they are developed or originated by the mortgage loan seller or servicer or others. The mortgage loan originator, seller, or servicer; any service bureau; or any other party providing services in connection with servicing a mortgage loan for, or delivering a mortgage loan to, Fannie Mae will have no right to possession of these documents and records except under the conditions specified by Fannie Mae. Any of these documents and records in possession of the mortgage loan originator, seller, or servicer, any service bureau, or any other party providing services in connection with selling a mortgage loan to, or servicing a mortgage loan for, Fannie Mae are retained in a custodial capacity only." Freddie Mac's Servicing Guide at § 52.5 similarly provides:	

182

TOPIC	ISSUE	RECOMMENDATION
	"All documents in the Mortgage file, all data related to Mortgages owned or guaranteed by Freddie Mac to which the Servicer obtains access in connection with any agreement with Freddie Mac, including, without limitation, data in the documents in the Mortgage file (collectively, Mortgage data) and all other documents and records related to the Mortgage of whatever kind or description (whether prepared or originated by the Servicer or others, or whether prepared or maintained or held by the Servicer or others acting for and on behalf of the Servicer), including all current and historical computerized data files, will be, and will remain at all times, the property of Freddie Mac. All of these records and Mortgage data in the possession of the Servicer are retained by the Servicer in a custodial capacity only. . . . Except as expressly authorized by Freddie Mac in writing, Servicers may not use or disclose, or authorize or permit third parties to use or disclose, these records or Mortgage data for any other purpose, including, without limitation, resale or licensing of Mortgage data, either alone or with other data."	
73. Informing borrowers of how to submit error assertions and information requests, § 38(b)(5)	Section 38(b)(5) requires servicers to have policies and procedures reasonably designed: "to ensure that the servicer informs borrowers of the procedures for submitting written notices of error set forth in § 1024.35 and written information requests set forth in § 1024.36." Comment 38(b)(5)-1 provides that servicers may comply: "by including in the periodic statement . . . a brief statement informing borrowers that borrowers have certain rights under	These appear inconsistent. The regulation is limited to informing borrowers of how to submit error assertions and information requests. The comment appears to also require informing consumers of their rights to submit error assertions and information requests and how to learn more about their rights. It also appears to require making available a description of the applicable procedures, nit just for submitting, but also for processing and responding to error assertions and information requests. We suggest that the CFPB rather than servicers is in a position to inform borrowers of their legal rights. We recommend that servicers be

TOPIC	ISSUE	RECOMMENDATION
	Federal law related to resolving errors and requesting information about their account, and that they may learn more about their rights by contacting the servicer, and a statement directing borrowers to a Web site that provides a description of the procedures set forth in §§ 1024.35 and 1024.36. Alternatively, a servicer may also comply with § 1024.38(b)(5) by including a description of the procedures set forth in §§ 1024.35 and 1024.36 in the written notice required by § 1024.35(c) and § 1024.36(b)."	required to inform consumers of how to submit error assertions and information requests, which certainly would indicate that they can do so. We suggest that this should be sufficient.
74. Compiling servicing file in five days, § 38(c)(2)	Section 38(c)(2) requires servicers to retain certain information "in a manner that facilitates compiling such documents and data into a servicing file within five days[.]"	The five-day requirement should mean business days and not calendar days. If it is calendar day and a there is a weekend or a holiday during the five days, the servicer could have as little as two days to compile the information, which is unreasonably short.
75. Servicer's notes as part of the servicing file, § 38(c)(2)(iii)	Section 38(c)(2)(iii) defines the servicing file to include: "Any notes created by servicer personnel reflecting communications with the borrower about the mortgage loan account[.]" In some circumstances, a servicer may be required to produce this information. However, servicers' notes may not be in language plain enough for consumers to understand.	If a servicer is required to produce its notes to a consumer, we request clarification that the servicer may produce a summary of its notes, or a "translation" into plain language.
76. Report of data fields, § 38(c)(2)(iv)	Section 38(c)(2)(iv) requires servicers to maintain and to be able to access: "To the extent applicable, a report of the **data fields** relating to the borrower's mortgage loan account created by the servicer's electronic systems in connection with servicing practices[.]" The section-by-section analysis explains that this:	We recommend that if a servicer maintains data in a manner that facilitates accessing, within five business days, each data field for each loan, the servicer should be deemed in compliance. Preparing or printing a report of the data fields should not be required. It should be clear that § 38 and the requirement to report all data fields is for the purpose of servicer access to data and for reporting to examiners only.

TOPIC	ISSUE	RECOMMENDATION
	"[M]eans a report listing the relevant data fields by name, populated with any specific data relating to the borrower's mortgage loan account." 78 Fed. Reg. 10696, 10787 (February 14, 2013). The purpose of this requirement is unclear. It appears to be designed so that servicers and CFPB examiners will have access to loan data. If this is so, then the purpose or requiring a "report listing the relevant data fields" appears unnecessary. If a servicer needs to know, for example, the current escrow balance on a loan, the servicer's staff knows how to find that information. What is the purpose of a report that "we store escrow account balances for escrowed loans"? The reference to "data fields" is problematic because it is overbroad and vague. The term encompasses thousands of data elements without limitation. It is unclear why servicers who have access to their data should be required to create a new report of data fields. In a supervisory case, if the CFPB finds that a servicer cannot access data it needs, then perhaps a report may be appropriate. Otherwise, this provision seems an exercise in creating unnecessary paperwork without addressing an identified problem.	It should be clear that §§ 38 and 36 do not require servicers to provide all the data fields to a borrower who requests a servicing file. We urge the CFPB to indicate in Official Staff Commentary that requiring a servicing file that identifies **all, or even a number of, data fields** would be an overbroad and unduly burdensome request, and may include proprietary information. If the CFPB expects that servicers will provide information about the data fields to the borrower, limitations must be placed on the requirement. We request that servicers be required to provide the borrower with only those data fields necessary to resolve an error request or necessary to answer a specific information request (*e.g.* the servicer need only accesses the data necessary to answer the question, but need not provide all data fields upon request). Proprietary, confidential, privileged or protected information should never be required to be disclosed.
77. Data fields – timing § 38(c)(2)(iv)	Section 38(c)(2)(iv) requires servicers to maintain and to be able to access: "To the extent applicable, a report of the **data fields** relating to the borrower's mortgage loan account created by the servicer's electronic systems in connection with servicing practices[.]"	Servicers should be able to provide the information in the data fields as of a specific date if that is all that is required to respond to the servicer's needs or to the examiner.

185

TOPIC	ISSUE	RECOMMENDATION
	What point in time must be reflected in the "report of the data fields[?]"	
78. January 10, 2014 compliance date, comment 38(c)(2)-1	Comment 38(c)(2)-1 provides that the servicing file requirement does not apply retroactively: "A servicer complies with § 1024.38(c)(2) if it maintains information in a manner that facilitates compliance with § 1024.38(c)(2) beginning on or after January 10, 2014. A servicer is not required to comply with § 1024.38(c)(2) with respect to information created prior to January 10, 2014." This is certainly helpful, but does not address situations when a servicer is unable to obtain records, such as when a transferee acquires servicing from a bankrupt transferor servicer.	Servicers should not be required to maintain information they are unable to obtain. If a transferor servicer fails to or is unable to transfer relevant information, the transferee should not be in violation of any law, whether the information was created before or after January 10, 2014.
Early Intervention, § 39		
79. Live contact within day 36 of delinquency, § 39(a)	Section 39(a) provides: "A servicer shall establish or make good faith efforts to establish live contact with a delinquent borrower not later than the 36th day of the borrower's delinquency[.]" Comment 39(a)-1.i explains: "Delinquency begins on the day a payment sufficient to cover principal, interest, and, if applicable, escrow for a given billing cycle is due and unpaid, even if the borrower is afforded a period after the due date to pay before the servicer assesses a late fee."	We request clarification that the servicer need not attempt to establish live contact for each delinquent payment in a continuing delinquency. We request clarification that servicers have flexibility to comply with investor requirements that differ from the regulation in the event of a disaster.

TOPIC	ISSUE	RECOMMENDATION
	If there is a disaster and an investor instructs a servicer of loans in the area to cease collection-related communication for a period of time, this could conflict with the regulation.	
80. Date of delinquency after servicing transfer, comment § 39(a)-1.iii	Comment 39(a)-1.iii provides: "During the 60-day period beginning on the effective date of transfer of the servicing of any mortgage loan, a borrower is not delinquent for purposes of § 1024.39 if the transferee servicer learns that the borrower has made a timely payment that has been misdirected to the transferor servicer and the transferee servicer documents its files accordingly."	It is helpful that this applies only if the transferee is aware that the borrower made a timely payment to the transferor. A transferee should be required to treat only one misdirected payment from the same borrower as timely. There is no need to notify borrowers repeatedly of the same information. One misdirected payment may be an error, but the second one likely is not. The borrower may assume that the transferor will not cash the check, meaning mailing a check that would bounce to the transferor is a method to avoid having a delinquent payment treated as delinquent. The requirement that the transferee treat a payment as timely even when the servicer has not received it should never apply to any of the servicer's duties to investors, it should only apply to the servicer's duties with regard to the borrower. We recommend a comment making this clear.
81. Good faith efforts to establish live contact, comment 39(a)-2	Comment 39(a)-2 provides, in part: "Good faith efforts to establish live contact consist of reasonable steps under the circumstances to reach a borrower and may include telephoning the borrower on more than one occasion or sending written or electronic communication encouraging the borrower to establish live contact with the servicer." This standard is vague. Not only does it not define what the servicer	We recommend clarification that a servicer is deemed to have made a "reasonable effort" to solicit a borrower if over a period of at least 30 calendar days the servicer made a minimum of four telephone calls to the last known phone numbers of record, at different times of the day.

TOPIC	ISSUE	RECOMMENDATION
	must do, it does not identify which "circumstances" are relevant.	
82. Promptly informing borrowers of loss mitigation options, comment 39(a)-3.ii	Servicers must attempt to make live contact within 36 days of delinquency. Comment 39(a)-3.ii provides: "[T]he servicer must provide [loss mitigation] information promptly after the servicer establishes live contact. A servicer need not notify a borrower about any particular loss mitigation options at this time; if appropriate, a servicer need only inform borrowers generally that loss mitigation options may be available. If appropriate, a servicer may satisfy the requirement in § 1024.39(a) to inform a borrower about loss mitigation options by providing the written [45-day delinquency] notice required by § 1024.39(b)(1), but the servicer must provide such notice promptly after the servicer establishes live contact." This does not make clear when it is "appropriate" to include the information on loss mitigation options in the 45-day delinquency notice.	We recommend additional clarity. • It should be permissible to mail information on loss mitigation options within five days of establishing live contact. • If the servicer is unable to make live contact because the borrower does not respond to outreach, it should be permissible to send information on loss mitigation options within five business days of the 45-day delinquency notice.
83. Authenticating an agent before providing information on loss mitigation options, comment 39(a)-4	Comment 39(a)-4 provides: "Section 1024.39 does not prohibit a servicer from satisfying the requirements § 1024.39 by establishing live contact with and, if applicable, providing information about loss mitigation options to a person authorized by the borrower to communicate with the servicer on the borrower's behalf. A servicer may undertake reasonable procedures to determine if a person that claims to be an agent of a borrower has authority from the borrower to act on the borrower's behalf, for example, by requiring a person that claims to be an agent of the borrower provide documentation from the borrower stating	The time servicers spend waiting for a borrower or agent to provide information verifying the agent's authority should not count against the servicer's compliance with the requirement to make live contact or to send the 45-day delinquency notice. This recommendation is the same treatment in comments 35(a)-1 and 36(a)-1, relating to the time to respond to error assertions and information requests. Those comments permit servicers to treat the error assertion or information request as received "[u]pon receipt of such documentation" from the borrower that the agent has authority to act on the borrower's behalf. It is also similar to Regulation Z comment

TOPIC	ISSUE	RECOMMENDATION
	that the purported agent is acting on the borrower's behalf."	36(c)(3)-1, which permits creditors to verify the authority of an agent who requests a payoff statement before the time for delivering a payoff statement begins to run.
84. One notice during 180 days, § 39(b)(1)	Section 39(b)(1) requires a written notice within 45 days of a loan becoming delinquent. It also provides: "A servicer is not required to provide the written notice more than once during any 180-day period." If a servicer mails a 45-day delinquency notice on February 15, the borrower comes current on March 1, and does not make the April 1 or May 1 payments, is a new 45-day delinquency notice required?	We request clarification that a written notice is not required more that once during any 180-day period, even if the borrower cures and redefaults one or more times during the 180 days. We request clarification that a servicer need only provide one 45-day delinquency disclosure if the borrower remains delinquent, for example, for 300 consecutive days because that borrower is only 45-days delinquent once. We request clarification that, if the loan in the example were to remain delinquent, the second notice must be mailed on or before 180 days after February 15.
85. Incorrect cross-reference, § 39(b)(1)	The reference in § 39(b)(1) to "paragraph (a)(2)" means paragraph (b)(2).	
Continuity of Contact, § 40		
86. Authenticating an agent before assigning personnel and assisting borrower through agent, comment 40(a)-1	Comment 40(a)-1 provides: "A servicer may undertake reasonable procedures to determine if a person that claims to be an agent of a borrower has authority from the borrower to act on the borrower's behalf, for example by requiring that a person who claims to be an agent of the borrower provide documentation from the borrower stating that the purported agent is acting on the borrower's behalf."	The time servicers spend waiting for a borrower or agent to provide information verifying the agent's authority should not count against the servicer's compliance with the requirement to assign personnel and begin assisting the agent. This recommendation is the same treatment in comments 35(a)-1 and 36(a)-1, relating to the time to respond to error assertions and information requests. Those comments permit servicers to treat the error assertion or information request as received "[u]pon receipt of

TOPIC	ISSUE	RECOMMENDATION
		such documentation" from the borrower that the agent has authority to act on the borrower's behalf. It is also similar to Regulation Z comment 36(c)(3)-1, which permits creditors to verify the authority of an agent who requests a payoff statement before the time for delivering a payoff statement begins to run.
87. Two consecutive payments without a late charge, § 40(a)(2)	Section 40(a)(2) requires servicers to make contact personnel available: "[U]ntil the borrower has made, without incurring a late charge, two consecutive mortgage payments in accordance with the terms of a permanent loss mitigation agreement."	We request clarification that this means that the borrower did not incur a late charge because the two consecutive payments were made in time or within any grace period, and not that the servicer is required to waive applicable late fees after a permanent modification.
88. Complete payment history, § 40(b)(2)(i)	Section 40(b)(2)(i) requires servicers to maintain policies and procedures reasonably designed to ensure that the personnel assigned to a delinquent borrower are able to timely retrieve a "complete record of the borrower's payment history[.]" This presumes the complete history will always be available, but it may not be.	Servicers should not be required to retrieve information they are not able to obtain. This provision should be consistent with: • Section 38(c)(2)-1, which provides that the servicing file requirement does not apply retroactively. • Comment 39(a)-1.iii, which acknowledges that a transferor servicer may not be aware of a payment sent to the transferee within 60 days of a servicing transfer. • The possibility that a transferor servicer may be unable to transfer relevant information.
89. Providing error assertion information, § 40(b)(4)	Section 40(b)(4) provides: "A servicer shall maintain policies and procedures reasonably designed to ensure that servicer personnel assigned to a delinquent borrower . . . [p]rovide a delinquent borrower with information about the procedures for submitting a notice of error pursuant to § 1024.35 or an information request pursuant to § 1024.36." It should not matter who provides the information, only that someone	We request clarification that this does not require a separate notice to every borrower to which personnel are assigned, by each of those assigned persons. We recommend that the servicer be permitted to provide the information in any reasonable manner, and that providing the information in a periodic statement or with a 45-day delinquency notice is *per se* reasonable.

190

TOPIC	ISSUE	RECOMMENDATION
	does.	
Loss Mitigation Procedures, § 41		
	See also the entry under § 31, Exceptions to the definition of loss mitigation option	
90. Number of days before foreclosure, § 41 generally	Section 41 sets several requirements and prohibitions based on the number of days before a foreclosure sale. This presumes the servicer knows precisely how many days until a foreclosure sale will occur, but this may not be the case. For example, § 41(b) requires servicers who receive incomplete loss mitigation applications to notify borrowers of the missing information, and of a deadline for submitting that information that may be based on the date that is 38 or 90 days before a foreclosure sale. The servicer will not know this date. A notice under § 41(b)(2)(i)(B) to the borrower that there is a deadline for completing the application, but that the servicer does not know the deadline, would be required but would also be more confusing than helpful. Suppose a servicer notifies a borrower on March 5 that the deadline is June 1, which is the date on which the financials become stale under § 41(b)(2)(ii)(a), and no foreclosure is yet scheduled. If on March 30, the servicer learns that a foreclosure sale is scheduled for April 30, the application deadline would be advanced. This will cause the borrower to feel cheated, and UDAAP litigation is a likely result, although the servicer did as the regulation directed. Moreover, the servicer in this case could be found to have violated the regulation for having sent a notice that did not state "the earliest remaining date" within the meaning of § 41(b)(2)(ii). This regulation requires servicers to do the impossible, and attaches liability for noncompliance. This is	We very strongly urge the CFPB to amend its regulation to measure time periods with certainty. There should be no litigation over servicers' ability to predict foreclosure sale dates. There should be no notices that confuse or misinform borrowers. The regulation should not interfere with servicers' ability to meet GSE requirements.

TOPIC	ISSUE	RECOMMENDATION
	fundamentally unfair. The section-by-section analysis explains: "For example, § 1024.41 imposes requirements with respect to complete loss mitigation applications received more than 37 days before a foreclosure sale. This is consistent with the National Mortgage Settlement and GSE requirements." 78 Fed. Reg. 10696, 10822 (Feb. 14, 2013). The regulation measures time quite differently than the 50-state settlement agreement, the GSEs, or FHA. Notably, the 50-state settlement, the GSEs, and FHA do not use unknown dates in setting their timeframes. The following are apparent inconsistencies between the regulation and the GSE requirements: • Section 41(c)(1) requires evaluation of a complete loss mitigation application within 30 days, if the servicer receives it more than 37 days before a foreclosure sale even if the date of the sale is unknown. The GSEs require the same if the application is received before a foreclosure referral; but if the application is received after the referral, whether the GSEs permit 30 days to evaluate the application depends on the scheduled foreclosure sale. If an application is received when a foreclosure sale date is unknown, the requirements appear inconsistent. The regulation appears to require the servicer to know the unknown. If a servicer assumes that a foreclosure is more than 37 days away and begins to evaluate an application, and within 15 days learns that the foreclosure sale is 14 days away, what is required is unclear.	

TOPIC	ISSUE	RECOMMENDATION
	• Both GSEs require foreclosure referrals by day 120 of delinquency in most cases, and penalize servicers for noncompliance. The CFPB's regulation needs to permit compliance with the GSEs' requirements. Specifically, if a borrower submits an incomplete loss mitigation application at 110 days delinquent (10 days before the GSEs require a foreclosure referral), the servicer continues to try to obtain missing information but the borrower does not provide it, the servicer should be permitted to refer the loan to foreclosure on day 120. Section 41(c)(2)(ii) seems to imply that the servicer must wait "for a significant period of time under the circumstances" for the borrower to complete the application. Ten days may not be "a significant period of time" and the regulation appears inconsistent with the GSEs' requirements. • Section 41(f)(1) prohibits servicers from making the "first notice or filing" (a vague term, as discussed below) until the loan is "more than" 120 days delinquent. The GSEs usually require a foreclosure referral by day 120, a day earlier than the regulation apparently permits. This is not workable. • Section 41(g) prohibits moving for a foreclosure sale if the borrower submits a complete application after the first notice or filing and more than 37 days before a foreclosure sale, even if that sale date is unknown. This requires compliance with the unknown. The GSEs do not require a delayed foreclosure action if a complete application is received 38 or more days before a scheduled foreclosure sale because there is enough time to review the application and to complete the pre-foreclosure certification. *See* Fannie Mae's Aril 25, 2012 revision to Announcement 2011-08R, FAQ 37. • There is no GSE requirement that servicers identify a date in any notice that could potentially "spring back" and make the notice	

TOPIC	ISSUE	RECOMMENDATION
	inaccurate after the consumer receives it and, potentially, detrimentally relies on it. A significant difference between the regulation and the requirements of the 50-state settlement, the GSEs, and FHA is that the regulation creates a private right of action under § 41. Penalties for noncompliance with the 50-state settlement and the GSE and FHA requirements exist, but only when the servicer does not comply with known requirements. Under § 41, liability for a servicer's inability to guess foreclosure sale dates, sometimes 90 days into the future, will result. Litigation over blind guesses of events far off into the future would be unreasonable, and the cost of that litigation would need to be included in the future cost of consumer mortgage credit.	
91. Submitting or receiving applications, § 41 generally	Section 41(f)(2) and (g) use the phrase "a borrower submits a complete loss mitigation application" but elsewhere the regulation uses the phrase "servicer receives" a complete loss mitigation application or something similar. *See* § 41(b)(1), (b)(2)(i), (c)(1), (e)(1).	We request clarification that there is no difference between the similar phrases, and that an application is not complete until the servicer actually receives everything the servicer requires the borrower (or the borrower's agent) to submit.
92. Evaluations in the servicer's discretion, § 41(a) and comment 41(c)(1)-1	Section 41(a) provides: "A borrower may enforce the provisions of this section pursuant to section 6(f) of RESPA (12 U.S.C. 2605(f)). Nothing in § 1024.41 imposes a duty on a servicer to provide any borrower with any specific loss mitigation option. Nothing in § 1024.41 should be construed to create a right for a borrower to enforce the terms of any agreement between a servicer and the owner or assignee of a mortgage loan, including with respect to the evaluation for, or offer of, any loss mitigation option or to eliminate any such right that may exist pursuant to applicable law."	We request clarification that state attorneys' general and federal or state regulators cannot enforce § 41 because they are not "a borrower" under § 41(a). The CFPB should state explicitly in a comment that failure to allow loss mitigation options is in no circumstance a breach of a mortgage loan contract with a borrower, a violation of Regulation X, a UDAP, or a UDAAP.

TOPIC	ISSUE	RECOMMENDATION
	Comment 41(c)(1)-1 provides: "The conduct of a servicer's evaluation with respect to any loss mitigation option is in the sole discretion of a servicer. A servicer meets the requirements of § 1024.41(c)(1)(i) if the servicer makes a determination regarding the borrower's eligibility for a loss mitigation program. Consistent with § 1024.41(a), because nothing in section 1024.41 should be construed to permit a borrower to enforce the terms of any agreement between a servicer and the owner or assignee of a mortgage loan, including with respect to the evaluation for, or provision of, any loss mitigation option, § 1024.41(c)(1) does not require that an evaluation meet any standard other than the discretion of the servicer." This comment is quite helpful.	
93. Definition of loss mitigation application, § 41(b)(1)	Comment 41(c)(2)(i)-1 states that nothing in § 41(c)(2)(i) prohibits a servicer from offering loss mitigation options to a borrower who has not submitted a loss mitigation application. "For example, if a servicer offers trial loan modification programs to all borrowers who become 150 days delinquent without an application or consideration of any information provided by a borrower in connection with a loss mitigation application, the servicer's offer of any such program does not violate § 1024.41(c)(2)(i), and a servicer is not required to comply with § 1024.41 with respect to any such program, because the offer of the loss mitigation option is not based on an evaluation of a loss mitigation application."	A servicer may offer a modification based on, instead of a complete application, a certain number of days delinquent, a FICO score, and/or the property being within an acceptable federally declared disaster area. In this case, must the servicer evaluate the borrower for all loss mitigation options pursuant to § 41(c)? Does the response change if the servicer requires a signed hardship affidavit?

195

TOPIC	ISSUE	RECOMMENDATION
94. Reasonable due diligence, § 41(b)(1)	Section 41(b)(1) provides: "A servicer shall exercise reasonable diligence in obtaining documents and information to complete a loss mitigation application." Comment 41(b)(1)-4.I gives as an example of reasonable diligence: "A servicer requires additional information from the applicant, such as an address or a telephone number to verify employment; the servicer contacts the applicant promptly to obtain such information after receiving a loss mitigation application[.]" This acknowledges the fact that the initial notice may not be able to include each piece of information conceivably required to complete an application. In five days, the servicer will have time for an initial review, but not time for full underwriting. Underwriters may later determine additional information is required.	Two notices need to be permitted. The first notice is early, within 5 days, but is therefore limited to an initial review. Thereafter, the servicer may determine that more specific information is required. The servicer should be permitted to request the more specific information after the initial notice, as long as the initial notice listed all information the servicer then knew would be required to make the application complete. We request clarification that placing a notice in the mail that states what then-known information is missing, within five days of receipt of an incomplete application, is reasonable due diligence within the meaning of § 41(b)(1). We recommend that a servicer later be able to notify the borrower of additional underwriting information that is required. If this is not permitted, the servicer would need to be able to deny the application because the servicer cannot determine whether the application met investor mitigation requirements. We recommend adding to the commentary that one example of reasonable diligence is sending two letters following up on the missing documents. This standard is consistent with Treasury's HAMP program.
95. Notice of missing application information and application deadlines, §§ 41(b)(2)(i)(B) and 41(b)(2)(ii)	Section 41(b)(2)(i)(B) requires servicers to notify borrowers within five business days of any information missing from a loss mitigation application, if the servicer receives a complete application more than 45 or more days before a foreclosure sale. Section 41(b)(2)(ii) notices: "[M]ust state that the borrower should submit the documents and	There needs to be certainty about the deadline for completing loss mitigation applications. Given that the rule requires a notice of default at day 45 of delinquency, and that starting a foreclosure is prohibited before day 121 of delinquency, borrowers will have at least 76 days to complete a loss mitigation application. This is more than ample time, so there is no reason for unworkable rules.

TOPIC	ISSUE	RECOMMENDATION

	information necessary to make the loss mitigation application complete by the earliest remaining date of:
	(A) The date by which any document or information submitted by a borrower will be considered stale or invalid pursuant to any requirements applicable to any loss mitigation option available to the borrower;
	(B) The date that is the 120th day of the borrower's delinquency;
	(C) The date that is 90 days before a foreclosure sale; or
	(D) The date that is 38 days before a foreclosure sale."
	
	There are several issues with this notice requirement:
	• The servicer may not know whether the borrower submitted the information 45 or more days before a foreclosure sale, and therefore may not know whether the notice is required.
	• If the foreclosure sale date is unknown but the servicer sends a notice stating that the deadline is, for example, under (A), 75 days in the future, but a foreclosure sale is thereafter scheduled for a date earlier than the deadline the servicer gave the borrower, the notice would be more confusing than helpful.
	  ○ In this event, does the rule require a servicer to postpone the foreclosure sale?
	  ○ If so, may servicers set the date at which documents become stale as the earlier of X days or the date of a scheduled foreclosure sale?
	• Deadlines (C) and (D) will often be unknown. If a servicer must tell a borrower that the deadline is 90 or 38 days before a foreclosure and that the servicer does not know what date that is, the notice would be more confusing than helpful.
	• Requiring servicers to send a potentially inaccurate or misleading
		We do not object to permitting borrowers to submit non-duplicative, complete applications late in a delinquency. However, the requirements for evaluating these applications need to be defined by known deadlines.
		
		We recommend:
		• Removing the requirement to identify the list of four dates.
		• Incomplete applications should not delay otherwise appropriate foreclosures. Otherwise, incomplete applications would become an easy tool for delaying otherwise appropriate foreclosures. Especially given that the borrower has already had ample time, this should be unnecessary.
		• Non-duplicative, complete applications submitted after the 90th day of delinquency should not delay a foreclosure. Evaluation of these late applications should be required only if there is time to evaluate the application before a scheduled foreclosure sale date.
		• Servicers should be permitted to set reasonable deadlines for receipt of a complete application, such as:
		  ○ The 90th day of a delinquency; and
		  ○ The earlier of (i) 38 days before a *scheduled* foreclosure sale, or 30 days after a notice of missing documents. These dates would vary depending on how close to foreclosure the borrower is (*e.g.* a 30-day timeline for the borrower to return missing documents may not be reasonable if judgment and/or the scheduling of the foreclosure sale by the court are pending). Diligent borrowers will complete their applications within day 90 of delinquency. If they wait until later, they risk losing the opportunity to appeal a modification denial, and they risk not

TOPIC	ISSUE	RECOMMENDATION
	disclosure is a disservice to the borrower and could subject the servicers to liability. A more appropriate disclosure is warranted. Section 205.04 of Fannie Mae's Guide provides that the stale date of documents is determined from the date of a complete application: "The borrower's income must be supported by documentation that is not more than 90 days old as of the date the servicer first determines that the borrower submitted a complete Borrower Response Package [application]." Freddie Mac's guide is similar. *See* § 65.18(a).	having time for evaluation of their application. Servicers should not have to delay foreclosure for delayed actions of the borrower. • Failure to complete an application timely will render the application dormant, but not declined. Servicers are still free to consider the application, but will have some certainty in designing compliance procedures. • If the borrower submits an incomplete application, notice to the borrower of what is missing should also state: o The borrower should complete the application as soon as possible; o The servicer will need 30 days to evaluate the application after it is complete; o If a foreclosure sale is scheduled before the 30-day evaluation period, the servicer may not be able to complete its evaluation. • Servicers should be permitted to provide a generic statement of when documents become stale. A statement that "the documents you submit remain current and we can use them for 90 to 120 days after their effective date" should suffice. Otherwise the disclosure could get unworkably long because the borrower may have submitted, for example, a bank statement dated February 1, a paystub dated March 1, and different stale dates may apply to different documents. Five days may be too short to compile a complete list of the expiration date of each document. We recommend that a general warning that delays in completing an application could cause documents to become too old, and could require the borrower to submit updated information. • Servicers should be able to encourage borrowers to submit their applications as soon as possible. If the stale date of documents is

TOPIC	ISSUE	RECOMMENDATION
		based on the date of a complete application (as with the GSEs), the servicer will not know that date. In this case, servicers should not be required to notify borrowers of a specific stale date. • We do not object to disclosures about the foreclosure timelines, but we cannot support requiring disclosures that servicers do not know how to complete. Any timeline disclosures should be general, and it should be permissible to state that some of the events may have already passed. • If a servicer notifies a borrower of missing information and the borrower thereafter supplies some, but not all, of the specified information, a second notice should be permissible, but not required because it would be redundant. • If a borrower does not submit the specified information by the deadline, servicers should be permitted to close the request due to incomplete information. This would not preclude the borrower from completing the application later if there is time for the servicer to evaluate the application. • The required notice of missing information should be restricted to then-relevant information. For example, if a borrower applies for a loan modification, the servicer should only tell the borrower of any missing information needed for a modification application. If the servicer does so, but the borrower does not obtain a modification, and later applies for a short sale, the earlier communication of missing modification information should not be a violation. This would seem consistent with comment 41(c)(1)-3, which permits servicers to require additional third-party information for a non-home retention option.
96. Must or should submit	Section 41(b)(2(i)(b) provides that when a borrower submits an	The purpose of this notice is to communicate that failure to complete an

199

TOPIC	ISSUE	RECOMMENDATION
documents, § 41(b)(2)(i)(B) and (b)(2)(ii)	incomplete application, the servicer must notify the borrower of: "the additional documents and information the borrower *must* submit to make the loss mitigation application complete . . . ." Section 41(b)(2)(ii) requires the same notice to: "state that the borrower *should* submit the documents and information necessary to make the loss mitigation application complete . . . ."	application by a deadline would have negative consequences for the borrower. The servicer should be able to communicate this in clear language. A notice that the borrower should complete the application as soon as possible, and must complete it in time for the servicer to be able to evaluate it, would be appropriate.
97. Evaluation for all loss mitigation options available, § 41(c)(1)(i)	Section 42(c)(1)(i) provides that, in some circumstances, a servicer that receives a complete loss mitigation application must: "Evaluate the borrower for all loss mitigation options available to the borrower[.]" Comment 41(c)(1)-3 provides: "A servicer's offer of a non-home retention option may be conditional upon receipt of further information not in the borrower's possession and necessary to establish the parameters of a servicer's offer. For example, a servicer complies with the requirement for evaluating the borrower for a short sale option if the servicer offers the borrower the opportunity to enter into a listing or marketing period agreement but indicates that specifics of an acceptable short sale transaction may be subject to further information obtained from an appraisal or title search" These appear inconsistent.	We request clarification that there may be two evaluations. The initial evaluation, after receipt of a modification application, is for a trial or permanent modification. Thereafter, if no modification occurs, and if the borrower and property are eligible for a non-retention alternative, the servicer should be able to require additional information to evaluate a non-retention alternative. We also request clarification that if a servicer's or government agency's waterfall allows the servicer to by-pass home retention offers when the borrower does not want to retain the home, that servicers need not evaluate the borrower for home retention options. Similarly, if a borrower is uninterested in a modification, there should be no requirement to evaluate the borrower for a modification, or to notify the borrower of missing modification application information. FHA and other short-sale programs prohibit offering a short sale marketing period until an appraisal and title are complete. The rule implies that servicer must offer the marketing period first before the agencies' conditions are met. This forces servicers to be out of

TOPIC	ISSUE	RECOMMENDATION
		compliance with one of the rules.
98. Third party fails to submit required application information, § 41(c)(2)(ii), § 41(h) and § 38(b)(2)(v)	Section 41(c)(2)(ii) provides: "[I]f a servicer has exercised reasonable diligence in obtaining documents and information to complete a loss mitigation application, but a loss mitigation application remains incomplete for a significant period of time under the circumstances without further progress by a borrower to make the loss mitigation application complete, a servicer may, in its discretion, evaluate an incomplete loss mitigation application and offer a borrower a loss mitigation option." Section 38(b)(2)(v) requires servicers to have policies and procedures reasonably designed to ensure that servicers can: "Properly evaluate a borrower who submits an application for a loss mitigation option for all loss mitigation options for which the borrower may be eligible pursuant to any requirements established by the owner or assignee of the borrower's mortgage loan and, where applicable, in accordance with the requirements of § 1024.41." A servicer may receive all information required from a borrower but, due to reasons beyond a servicer's control, may not receive all information required from a third party. In this case, the servicer will not be able to evaluate the application.	Both of the cited provisions need to take into account the possibility that a servicer may receive all information required from a borrower but not from a third party. In this situation, we recommend that the servicer can elect to do any or all of the following: • Treat the application as incomplete for purposes of § 41(c), 41(f)(2) and 41(g), so that evaluation of the application is permissible but not required. • Treat the borrower as not eligible for the loss mitigation applied for within the meaning of § 38(b)(2)(v), because a "proper" evaluation is not possible. If a servicer denies an application for a modification and the borrower appeals, the servicer has only 30 days to decide the appeal. If the servicer requires third party information to determine an appeal but does not timely receive it, the servicer should be permitted to deny the appeal on that basis.
99. Denial notices, § 41(d)(1)	Section 41(d)(1) requires denial notices to state:	We request clarification that a summary of the primary reasons is sufficient.

TOPIC	ISSUE	RECOMMENDATION
	"If a borrower's complete loss mitigation option is denied for any trial or permanent loan modification option available to the borrower . . . a servicer shall state in the notice sent to the borrower . . . (1) The specific reasons for the servicer's determination for each such trial or permanent modification option[.]"	We request clarification that if a borrower or property do not meet basic modification eligibility criteria (*e.g.*, owner-occupancy), that the modification is not "available to the borrower." Otherwise, the servicer could be required in these cases to unnecessarily run the NPV analysis, calculate the DTI, and so on, and list these if they are additional reasons for denial. We request clarification of the procedure if a borrower is simultaneously approved for one modification and denied for another. • Is a denial notice required? • Is an appeal available? If so and the borrower appeals the denied modification, but the date for accepting the approved modification lapses while the appeal is pending, and the borrower loses the appeal, is the approved modification available to the borrower? • The servicer should be able to require the borrower to accept and comply with the approved loss mitigation option, pending appeal of a denied modification, or to reject the approved loss mitigation option. Otherwise, the terms of the offered mitigation could be materially altered by arrearages or tax or insurance payments.
100. First foreclosure notice or filing, § 41(f)(1), (f)(2), (g) (j), and § 35(b)(9)	Section 41(f)(1) and (j) prohibit making "the first notice or filing required by applicable law for any judicial or non-judicial foreclosure process" until a loan is 121 days delinquent. If a borrower submits a complete loss mitigation application within the first 120 days of delinquency, § 41(f)(2) prohibits the servicer from making "the first notice or filing required by applicable law for any judicial or non-judicial foreclosure" until the servicer processes the application. Section 41(g) in some cases prohibits moving for a foreclosure judgment or sale "after a servicer has made the first notice or filing	We suggest instead that the first notice or filing be limited to the first action required by law as defined by FHA, referred to as the **first public action** (*i.e.*, an action that will be publically available, even if time elapses before it actually becomes public): "HUD considers foreclosure instituted when the mortgagee takes the first public action required by law such as filing a complaint or petition, recording a notice of default, or publication of a notice of sale. Merely posting notice on the property is not sufficient. The

TOPIC	ISSUE	RECOMMENDATION
	required by applicable law for any judicial or non-judicial foreclosure process" if an application is pending. Section 35(b)(9) defines an error to include "[m]aking the first notice or filing required by applicable law for any judicial or non-judicial foreclosure process in violation of § 1024.41(f) or (j)." Comment 41(f)(1)-1 explains (emphasis added): "The first notice or filing required by applicable law refers to any document required to be filed with a court, entered into a land record, **or provided to a borrower** as a requirement for proceeding with a judicial or nonjudicial foreclosure process. Such notices or filings include, for example, a foreclosure complaint, a notice of default, a notice of election and demand, or any other notice that is required by applicable law in order to pursue acceleration of a mortgage loan obligation or sale of a property securing a mortgage loan obligation." This definition of the "first notice or filing" is unclear, contradictory, and unworkable, and is unrelated to nonpayment defaults. As amended, Regulation X requires a notice to a borrower who is 45 days delinquent. That 45-day delinquency notice is required before a servicer can foreclose, and therefore, that notice under § 41(e)(2) and (f)(1) could be the "first notice . . . required by applicable law . . . to a borrower" before proceeding with a foreclosure. That 45-day notice also appears to be a "notice of default" within the comment's list of examples of what the regulation prohibits. Thus, it appears that the required 45-day delinquency notice is prohibited before the loan is 121	action must be established as a public record through a filing, recording, or a publication in a newspaper of general circulation as required by law." HUD Claims Handbook 4330.4, Chapter 2-2 (1994). HUD's Mortgagee Letter 2005-30 lists "the first legal action necessary to initiate foreclosure on a mortgage and of the typical security instrument used in each state." This letter identifies as the "first legal action" only formal actions, such as a recorded notice of default, filing foreclosure documents with a public trustee, filing a complaint, publication in a newspaper of general circulation, and so on. Unlike § 41, FHA does not consider sending a notice to the borrower, alone, as the first notice or filing initiating a foreclosure. Fannie Mae does not use this "first legal action" standard, but instead requires that the loan be referred to an attorney (or trustee) to initiate foreclosure by the 120th day of delinquency, provided any applicable state law notice and waiting period is met. FNMA Announcement SVC 2011-08R (page 17). The first "public action" as defined by FHA above would generally occur after the referral to foreclosure attorney. Either the FHA or the GSE standard would be workable. The § 41 standard contradicts itself. It is critical that a clarification indicate that all of § 41 does not apply to nonpayment defaults.

TOPIC	ISSUE	RECOMMENDATION
	days delinquent. Regulation Z requires servicers to modify the periodic statement when a loan is 45 days delinquent by including additional information. This information similarly could fall within the meaning of the "first notice or filing," and appears to be a "notice of default" within the comment's list of examples of what the regulation prohibits. This 45-day requirement also appears to be prohibited until the loan is 121 days delinquent. Additionally, if a delinquent borrower calls a servicer about the default, it would be difficult for the servicer to avoid giving the borrower information about a default. In effect, the servicer could be "required" to provide "notice" of the default by phone, but that appears to be prohibited before the loan is 121 days delinquent. The requirement to attempt to establish live contact could also be a notice to a borrower required before proceeding with a foreclosure. Making personnel available by phone to a delinquent borrower apparently also is a notice to a borrower required before foreclosure. Section 41(f)(1) is not limited to written notices. Moreover, the definition appears to vary based on investor requirements. For example, if investor A offers no loss mitigation and investor B does, and B's borrower submits a loss mitigation application, the servicer is required to provide that borrower with a notice of receipt, notice of missing information, notice of any decision on the application, and so on. Each of these notices could be included within the meaning of first notice or filing and prohibited before the loan is 121 days	

204

TOPIC	ISSUE	RECOMMENDATION
	delinquent. Further, not all foreclosures are based on payment default. For example, a borrower may demolish the home and refuse to rebuild it, may sell the property to a friend or family member without the servicer's consent, or may store hazardous substances on the property, and thereby be in default even if all payments are timely. Nonpayment defaults should be completely exempt from § 41 because they are unrelated to the borrower's ability to pay, or to the benefit of loss mitigation options. These are examples of strategic defaults, not of need for consumer protection. Even if the "first notice or filing" were to exclude all RESPA and TILA notices, the contradictory requirements problem would remain because states and investors require various notices to delinquent borrowers before the loan is 121 days delinquent. FHA's regulations require certain servicer actions within time limits measured from the date of delinquency. FHA extends the time when state law or bankruptcy law prohibit the FHA timelines, but not when another federal law, such as Regulation X, prohibit the FHA timelines. Therefore, servicers cannot comply with both FHA and CFPB rules. 24 C.F.R. § 203.355(c) provides: "(c) *Prohibition of foreclosure within time limits.* If the laws of the State in which the mortgaged property is located, or Federal bankruptcy law: (1) Do not permit the commencement of foreclosure within the time limits described in paragraphs (a), (b), (g), (h) and (i) of this section,	

TOPIC	ISSUE	RECOMMENDATION
	the mortgagee must commence foreclosure within 90 days after the expiration of the time during which foreclosure is prohibited; or (2) Require the prosecution of a foreclosure to be discontinued, the mortgagee must recommence the foreclosure within 90 days after the expiration of the time during which foreclosure is prohibited."	
101. Preforeclosure referral or filing, § 41	The heading to § 41(f), but not the body of the regulation, refers to a prohibited foreclosure "referral." Section 41(f)(1) prohibits, not a referral, but only a first notice or filing, before day 121 of a delinquency.	We request confirmation that servicers may refer a loan to foreclosure counsel at any time, as long as the first notice or filing is not made impermissibly early. The GSEs often require referral to foreclosure by day 120 of delinquency, and this needs to remain permissible. A referral to foreclosure should not be a "first notice or filing."
102. No foreclosure filing for 120 days needs exceptions, § 41(f)(1), (f)(2), (g) (j), and § 35(b)(9)	If a borrower has vacated or surrendered a property, delaying a foreclosure would increase community blight, a disservice to everyone. Delaying a foreclosure would also unnecessarily impose property maintenance costs on the borrower.	We request clarification that after a borrower vacates or abandons a property, the property should be deemed not the borrower's principal residence within the meaning of § 30(c)(2), so that §§ 39 through 41 do not apply.
103. Appeals of offer or denial, § 41(h)	Section 41(h)(1) provides that borrowers may appeal denied modifications: "[A] servicer shall permit a borrower to appeal the servicer's determination to **deny** a borrower's loss mitigation application for any trial or permanent loan modification program available to the borrower." Section 41(h)(2) provides that borrowers have 14 days to appeal an offer: "A servicer shall permit a borrower to make an appeal within 14 days after the servicer provides the **offer** of a loss mitigation option	We request clarification that denials of modifications may be appealable, but offers of modifications are not appealable.

TOPIC	ISSUE	RECOMMENDATION
	to the borrower pursuant to paragraph (c)(1)(ii) of this section." Section 41(d) requires denial notices to include information about any appeal available.	
104. Appeals, § 41(h) and comment 41(b)(1)-2	Section 41(h) permits borrowers that submitted their complete applications at least 90 days before a foreclosure sale to appeal denial of "a borrower's loss mitigation application for any trial or permanent loan modification program available to the borrower." Comment 41(b)(1)-2 provides: "[I]f a borrower requests that a servicer determine if the borrower is 'prequalified' for a loss mitigation program by evaluating the borrower against preliminary criteria to determine eligibility for a loss mitigation option, the request constitutes a loss mitigation application."	We request clarification that: • A modification is not "available" when the property or loan are not eligible, such as if the property is not owner-occupied when owner-occupancy is required for a modification. • If the prequalification application is for a modification, a denial of the prequalification is not subject to appeal. If a borrower does not prequalify for a modification because, for example, the property is not owner-occupied, that modification is not "available to the borrower" under § 41(h). • A borrower's rejection of a modification offer is not appealable. • Acceptance of a modification offer, followed by a default on the modification, is not a denial subject to appeal.
105. Duplicative loss mitigation requests and the regulation's effective date, § 41(i) and comment 41(i)-1	Section 41(i) provides: "A servicer is only required to comply with the requirements of this section for a single complete loss mitigation application for a borrower's mortgage loan account." Comment 41(i)-1 provides: "A transferee servicer is required to comply with the requirements of § 1024.41 regardless of whether a borrower received an evaluation of a complete loss mitigation application from a transferor servicer."	We support reviewing applications for which loss mitigation is a realistic possibility, but we cannot support permitting loss mitigation applications, with private rights of action, for the purpose of delaying an inevitable foreclosure. We recommend that the CFPB clarify that § 41: • Does not apply retroactively. • Applies to borrowers who have been evaluated for loss mitigation before January 10, 2014 only if: o The borrower has demonstrated a material change in financial circumstances for a loss mitigation option, and The borrower has not been referred to foreclosure by January 10,

TOPIC	ISSUE	RECOMMENDATION
	For borrowers who have been evaluated before January 10, 2014 when the regulation becomes effective, this could be rather disruptive if those borrowers can be evaluated again. It could cause a spike in "new" applications, for which servicers would need to staff up temporarily, which would be operationally disruptive. Additionally, a second evaluation of a borrower who has been denied loss mitigation, or who breached a trial payment plan or a modification agreement, may violate investor requirements.	2014 under investor guidelines that do not require a second evaluation after foreclosure referral. If servicing is transferred after the transferor found a borrower ineligible to submit a new application, the transferee should not be required to accept a new application merely because of the fact of transfer.

208

TOPIC	ISSUE	RECOMMENDATION
Disclosures of Post Consummation Events, § 20		
106. Implementation date for rate reset notices, § 20(c) and (d)	Sections 20(c) and (d) require notices to borrowers based on the number of days until an adjustment will occur. How this will apply to loans for which the adjustment will occur shortly after January 10, 2014 is unclear.	We request clarification that §§ 20(c) and (d) do not require notices for loans that will adjust after January 10, 2014, but for which there is insufficient time to prepare and send the notices after January 10, 2014. Servicers should not need to begin complying with the regulation before it is effective. That is, when a notice is required X days before an adjustment, the notice should not be required if the adjustment occurs fewer than X days after January 21, 2014.
107. Coverage, § 20(c) and (d)	Section 20(c) requires rate reset notices when a rate adjustment results in a payment change. Section 20(c)(2) states when the notices are required for ARM loans. Sections 20(c)(1)(i) and (d)(1)(i) define an ARM loan to include only closed-end loans in which the APR may increase after consummation.	We request clarification whether § 20(c) or (d) notices are required for loans on which the APR may decrease but not increase after consummation.
108. Annual statement removed, § 20(c)	The amendments to § 20(c) remove the existing requirement to send annual statements when a rate adjusts but there is no payment adjustment.	We request clarification that continuing to send such disclosures will remain permissible.
109. Definition of adjustment, § 20(c)(2)	Section 20(c)(2) applies to loans: "[O]riginated prior to January 10, 2015 in which the loan contract requires the adjusted interest rate and payment to be calculated based on the index figure available as of a date that is less than 45 days prior to the **adjustment** date."	We request clarification of whether the two words "adjustment" in bold refer to the rate adjustment date or the payment adjustment date.

TOPIC	ISSUE	RECOMMENDATION
	It also requires disclosures: "[F]or the first **adjustment** to an ARM if it occurs within 60 days of consummation and the new interest rate disclosed at consummation pursuant to § 1026.20(d) was an estimate."	
110. Definition of last payment, § 20(c)(2)(ii) and 20(d)(2)(iii)(C)	Sections 20(c)(2)(ii) and 20(d)(2)(iii)(C) require a disclosure relating to interest-only or negative amortization payments, including how the current and new payments are allocated to principal, interest, and escrow. Both provide: "The current payment allocation disclosed shall be the payment allocation for the last payment prior to the date of the disclosure."	We request clarification of whether the "last payment" refers to the last scheduled payment or the last actual payment.
111. Step increases and trial or permanent modifications, § 20(c)(2)(iii) and (v)	Comment 20(c)-2 provides that rate reset notices are not required in connection with a loan modification, but that: "[S]ubsequent interest rate adjustments resulting in a corresponding payment change occurring pursuant to the modified loan contract, however, are subject to the requirements of § 1026.20(c)." It is common for rate reductions in HAMP permanent modifications to apply for five years, after which the rate can step up by up to one percentage annually until it reaches a cap. Comment 20(c)(1)(ii)-3.iii provides that § 20(c) does not apply to fixed-rate step-rate loans. Similarly, comment 20(d)(1)(ii)-2.iii provides that § 20(d) does not apply to fixed-rate step-rate loans. Section 20(c)(2)(iii) requires a disclosure of how the rate adjustment is determined, including: "(A) The specific index or formula used in making interest rate	We request model language to describe the rate adjustment and new payment after a modification if it is a step adjustment. For a loan that has a trial payment plan before it is modified, and the trial rate is lower than the pre-trial plan rate, is this adjustment "in connection with a modification" even there is no modification yet? If not, we request model language for the required disclosure. For a loan that has a trial payment plan at a reduced rate, but that is not permanently modified for any reason, the rate will revert to the pre-trial plan rate. Is a reset notice required regarding the rate reverting to a pre-trial plan rate although there is no modification? If so, we request model language.

210

TOPIC	ISSUE	RECOMMENDATION
	adjustments and a source of information about the index or formula; and (B) The type and amount of any adjustment to the index, including any margin and an explanation that the margin is the addition of a certain number of percentage points to the index, and any application of previously foregone interest rate increases from past interest rate adjustments." Section 20(c)(2)(v) requires a disclosure of how the new payment is determined, including: "(A) The index or formula used; (B) Any adjustment to the index or formula, such as the addition of a margin or the application of any previously foregone interest rate increases from past interest rate adjustments . . . ."	
112. Transactions permitting interest rate carryover, §§ 20(c)(2)(iv) and 20(d)(2)(v)	Sections 20(c)(2)(iv) and 20(d)(2)(v) require disclosure of: "Any limits on the interest rate or payment increases at each interest rate adjustment and over the life of the loan, as applicable, including the extent to which such limits result in the creditor, assignee, or servicer foregoing any increase in the interest rate and the earliest date that such foregone interest rate increases may apply to future interest rate adjustments, subject to those limits." Comment 20(c)(2)(iv)-1 provides: "Interest rate carryover, or foregone interest rate increases, is the amount of interest rate increase foregone at any ARM interest rate adjustment that, subject to rate caps, can be added to future interest	We request clarification that rate caps and floors and an indication that the interest rate is rounded are permitted disclosures on ARM notices even when the ARM loan does not provide for interest rate carryover.

TOPIC	ISSUE	RECOMMENDATION
	rate adjustments to increase, or to offset decreases in, the rate determined by using the index or formula. The disclosures required by § 1026.20(c)(2)(iv) regarding foregone interest rate increases apply only to transactions permitting interest rate carryover." Comment 20(c)(2)(ii)(A)-1 allows servicers to round the interest rate pursuant to the ARM contract. *See also* 20(d)(2)(iii)(A)-1 Can an interest rate floor adjustment, lifetime cap, and rounding factors be included or described in the ARM disclosures? The commentary implies lifetime caps and interest rate floors are only permitted on the ARM notices for interest rate carryover loans required under § 20(c) and (d). While the commentary indicates that rounding is permissible, there is no indication that such information may be included in the notices.	
113. Payment-option ARM loans, § 20(c)(2)(vi)	Section 20(c)(2)(vi) requires disclosure of: "If applicable, a statement that the new payment will not be allocated to pay loan principal and will not reduce the loan balance. If the new payment will result in negative amortization, a statement that the new payment will not be allocated to pay loan principal and will pay only part of the loan interest, thereby adding to the balance of the loan. If the new payment will result in negative amortization as a result of the interest rate adjustment, the statement shall set forth the payment required to amortize fully the remaining balance at the new interest rate over the remainder of the loan term."	We request clarification of whether the disclosure must include the allocation for the current and new minimum payment amounts; and whether the disclosure must include the allocation for each payment option, and if so, where. Examples of how these disclosures are to be completed would be most helpful.
114. Format, § 20(c)(3)	Section 20(c)(3) requires disclosures in a "format substantially similar	We request clarification of the types of changes that servicers can make

TOPIC	ISSUE	RECOMMENDATION
	to" the model forms.	to the model forms without jeopardizing the safe harbor. For example, for loans that will continue to have a "look back" period of less than 45 days, servicers will need to modify the language regarding the advance notice that will be given prior to payment changes. This should not jeopardize the safe harbor.
115. Timing of initial adjustment notice in a modification, § 20(d)	Section 20(d) provides: "The disclosures shall be provided to consumers at least 210, but no more than 240, days before the first payment at the adjusted level is due. If the first payment at the adjusted level is due within the first 210 days after consummation, the disclosures shall be provided at consummation."	We request confirmation that any initial adjustment notice required in connection with a modified loan, or a loan that has a trial payment plan regardless of whether the loan is permanently modified, may be delivered at the time of the modification (trial or permanent) offer, within 30 days after acceptance of a trial modification period, or within 30 days after execution and return of the modification agreement.
116. Assumptions, § 20(d)	Section 20(d) requires initial rate adjustment between 210 – 240 days before the first payment is due at the adjusted level.	A borrower who assumes a loan assumes all its terms and disclosures. We request clarification that the fact of an assumption does not alter the adjustment notice requirements.
117. Estimated initial rate adjustments, § 20(d)(2)	Initial rate adjustment notices may be required long before the rate adjustment is known.	Examples of how estimates are to be made would be quite helpful. Are disclosures to be based on worst-case assumptions about rate caps? If there is a cap on the first adjustment and a life-of-loan cap, must the servicer use the worst of the two?
118. Initial adjustment in a modification, § 20(d) and comment 20(d)-2	Section 20(d) requires a disclosure "in connection with the initial rate adjustment pursuant to the loan contract." Comment 20(d)-2 provides: "Under § 1026.20(d), the interest rate adjustment disclosures are required only for the initial interest rate adjustment occurring pursuant to the loan contract. Accordingly, creditors, assignees, and servicers need not provide the disclosures for interest rate adjustments occurring in loan modifications made for loss mitigation purposes. The initial interest rate adjustment occurring pursuant to	We request clarification of the following: • The distinction between the "adjustment occurring in [a] loan modification" and the "initial adjustment occurring pursuant to the modified loan contract." • If the first rate adjustment on a loan is the reduction with a trial payment plan, this is not a rate adjustment "pursuant to the loan contract" so that no initial adjustment disclosure is required. • If a rate is lowered for a trial payment plan and is contractually

TOPIC	ISSUE	RECOMMENDATION
	the modified loan contract, however, is subject to the requirements of § 1026.20(d)."	reduced with a permanent modification, this is not a rate adjustment "pursuant to the loan contract" so that no initial adjustment disclosure is required. • If a rate it reduced for a trial payment plan and the loan is not modified for any reason, so that the rate reverts to the pre-trial plan rate, this is not a rate adjustment "pursuant to the loan contract" so that no initial adjustment disclosure is required. • If an ARM loan rate adjusts, the loan is later modified with a second rate adjustment, and the rate later adjusts a third time, to which adjustment does § 20(d) apply?
119. Initial adjustment notice in a fixed-rate step-rate loan, comment 20(d)(1)(ii)-2.iii	Comment 20(d)(1)(ii)-2.iii provides that § 20(d) does not apply to fixed-rate step-rate loans.	We request clarification of whether § 20(d) applies to fixed-rate modified loans on which the rate may step up after a modification.
120.Disclosures of initial rate adjustments in modified loans, § 20(d)(2)(iv) and (vi)	If § 20(d) may apply in connection with trial or permanent loan modifications, how to disclose the initial rate adjustment will need clarity.	If any initial rate adjustment notices are required in connection with trial modifications or permanent modifications, we request model language for § 20(d)(2)(iv) and (vi) disclosures.
121. Modification as an alternative to a rate adjustment, § 20(d)(2)(x)	Section 20(d)(2)(x) requires disclosure of alternatives to a rate adjustment, including: "(C) Modifying the terms of the loan with the creditor, assignee, or servicer; and (D) Arranging payment forbearance with the creditor, assignee, or servicer."	We recommend that the servicer be permitted to qualify this language so as not to incorrectly cause the consumer to believe these options are available or likely available, for example by adding: "Not all loans qualify for modification or forbearance. You may call us if you would like to learn about these possibilities."
Prohibited Acts, §36		
122. Applicability to	Section 36(b) [in the LO compensation final rule] provides that § 36(c)	We request clarification of the applicability of § 36(c) to HELOCs.

TOPIC	ISSUE	RECOMMENDATION
HELOCs, § 36(b)	does not apply to HELOCs. Section 36(c)(3), relating to payoff statements, applies to "a consumer credit transaction secured by a consumer's dwelling[.]" The section-by-section analysis to the Regulation Z servicing rule provides: "[T]he Bureau believes it is appropriate to interpret TILA section 129G [payoff statements] to include HELOCs and other open-ended lines of credit secured by a consumer's dwelling in the payoff statement requirement." 78 Fed. Reg. 10902, 10957 (February 14, 2013).	
123. Partial payments, § 36(c)(1)(ii)	Section 36(c)(1)(ii) permits servicers to hold partial payment in suspense until there are sufficient funds to cover a periodic payment. This may not be consistent with an agreement a reinstated borrower makes to pay default fees over time. Servicers and borrowers should have flexibility to work out repayment of default fees. It does not accommodate trial plans, borrowers in bankruptcy whose payment amount has changed, and borrowers in foreclosure.	We request clarification of the following: • If a loan is in a trial plan, during which posting monthly payments is not required, posting payments should not be required. • For reinstated loans, servicers may hold funds in suspense that are greater than a contractual payment, but are intended to pay pending legal or other default fees as agreed until the default fees are paid. • For borrowers in bankruptcy, the payment amount may be greater than the pre-bankruptcy payment amount. In these cases, it should be permissible to hold funds in suspense until there is enough to make the bankruptcy payment amount. • For loans in foreclosure, is should be permissible to hold funds in suspense that are greater than a periodic payment. At this point, the loan is accelerated, so there is no periodic payment.
Periodic Statements, § 41		
124. Inapplicable to HELOCs, § 41(a)(1)	Section 41(a)(1) provides that § 41 applies only to closed-end loans.	We request clarification that this determination is made at origination. If a HELOC later becomes a closed-end loan, servicers may not have

TOPIC	ISSUE	RECOMMENDATION
		the capacity to produce all the periodic statement disclosures, including especially the transaction activity.
125. Definition of billing cycle, § 41(a)(1) and § 2(a)(4)	Section 41(a)(1) requires a periodic statement for each "billing cycle[.]" Comment 41(b)-1 provides that it may be provided "no later than" four days after the close of a courtesy period, although it may be provide earlier. Section 2(a)(4) defines billing cycle as: "[T]he interval between the days or dates of regular periodic statements. These intervals shall be equal and no longer than a quarter of a year. An interval will be considered equal if the number of days in the cycle does not vary more than four days from the regular day or date of the periodic statement." Assume the loan payments are due the 1st of the month and have a 15-day courtesy period. Assume a servicer sends a statement March 15. Assume the borrower then makes the April payment on April 5 and the servicer sends a statement on April 6 reflecting the April 5 payment and all activity since March 16. The April 6 statement also reflects the May payment due. Assume the borrower does not make the May payment until after the courtesy period, and a statement is generated May 17.	We request clarification that it is permissible for the servicer to send statements upon the earlier of receipt of a payment or within four days of a courtesy period, as § 41(a) appears to permit. In this example, the April 6 statement will cover March 16 through April 5 (21 days). The May 17 statement will cover April 6 through May 17 (42 days). Is this permissible even though the amount of time between statements varies by more than four days, because a statement within four days after the courtesy period is the "regular day or date" of the statement?
126. Timing of statement, comment 41(b)-1	Comment 41(b)-1 provides: "Delivering, emailing or placing the periodic statement in the mail within four days of close of the courtesy period of the previous billing cycle generally would be considered reasonably prompt."	We request clarification of the meaning of the word "generally." Are there circumstances when the periodic statement is required before four days after the courtesy period? We request confirmation that the four days are business days and not calendar days. Otherwise, on a three-day weekend, and especially

216

TOPIC	ISSUE	RECOMMENDATION
		without Saturday mail, there would not be enough time to prepare the statements.
127. Form of statements, § 41(c)	Section 41(c) provides that proper use of the model forms complies with § 41(c).	We request clarification of the types of changes that servicers can make to the model forms without jeopardizing the safe harbor. For example, can servicers provide more detail in the explanation of the amount due (§ 41(d)(2)(i)) to include the monthly amount needed to pay for optional products the borrower requested?
128. Layout of statement, § 41(d)	Section 41(d) requires highly prescriptive layout requirements. This will require costly retooling simply to move information to a different location without any substantive change. The costs are exceptionally high right now because servicers are currently implementing a great many other regulatory amendments. The cost is unreasonable in relation to any consumer benefit.	As long as the periodic statements are clear and conspicuous, servicers should be permitted to alter the layout. In the alternative, we request an extended compliance period for reformatting the periodic statements until servicers' implementation resources are not so overstretched. These would be almost no difference to consumers. We request an additional year.
129. Borrowers in bankruptcy, § 41(d)(2)	The regulation will require servicers to continue to provide periodic statements to borrowers in bankruptcy, while bankruptcy entails an automatic stay and requires collection activities to cease. The CFPB explains: "The Bureau understands that certain laws, such as the FDCPA or the Bankruptcy Code, may prevent attempts to collect a debt from a consumer in bankruptcy, but does not believe these laws prevent a servicer from sending a consumer a statement on the status of their loan. The final rule would allow servicers to make changes to the statement as they believe are necessary when a consumer is in bankruptcy; such servicers may include a message about the bankruptcy and alternatively present the amount due to reflect the payment obligations determined by the individual bankruptcy	Sending periodic statements may not technically violate the bankruptcy laws in some jurisdictions, but is inconsistent with their spirit and intent. In other jurisdictions, the rule may conflict directly with common law. We urge the CFPB not to put servicers at cross purposes to the bankruptcy courts. A simple disclaimer on what otherwise appears to be a debt collection notice may be insufficient to satisfy bankruptcy courts. In trustee "pay-all" jurisdictions, sending the periodic statements may confuse borrowers who must send all mortgage payments through the trustee. Section 41 should use language as in § 39(c) to the effect that nothing in § 41 requires communication with a borrower in a manner prohibited by applicable law.

TOPIC	ISSUE	RECOMMENDATION
	proceeding." 78 Fed. Reg. 10902, 10966 (February 14, 2013) (footnote omitted). Section 39(c), regarding live contact with delinquent borrowers, provides: "Nothing in this section shall require a servicer to communicate with a borrower in a manner otherwise prohibited by applicable law."	Servicers should be able to comply with any bankruptcy court orders. If a bankruptcy court orders a servicer to cease sending periodic statements, servicers should be able to comply with the court's order. We request clarification that when a servicer has a legal opinion or there is common law that sending a periodic statement would be inconsistent with applicable law, that the servicer need not send that periodic statement. The official staff commentary should restate what is in the preamble to ensure that this important clarification is part of the regulation. The preamble states: "The final rule would allow servicers to make changes to the statement as they believe are necessary when a consumer is in bankruptcy; such servicers may include a message about the bankruptcy and alternatively present the amount due to reflect the payment obligations determined by the individual bankruptcy proceeding." 78 Fed. Reg. 10902, 10966 (February 14, 2013). This clarification should also add that servicers may exclude information or not send a statement at all if providing the information or statement is inconsistent with common law or court orders or if the borrower is in Chapter 13 and in a trustee "pay-all" jurisdiction. At a minimum, the CFPB should be explicit that providing a periodic statement to a borrower in bankruptcy *per se* cannot be a UDAAP.
130. Explanation of amount due for delinquent borrowers, § 41(d)(2)	Assume the borrower's monthly payment is \$1000. Assume the borrower does not make the March payment within the courtesy period and a statement generated on March 18 reflects a late fee of \$50. For the "amount due" on the top of the first page of the March 18^{th} statement, the amount would be \$2050 (*i.e.* the March payment and the	The grouping at the top of the form should not be misleading. This one-line disclosure does not accommodate past due amounts, especially when there are more than one, so they should be included only elsewhere.

218

TOPIC	ISSUE	RECOMMENDATION
	current April payment plus the $50 late fee). The grouping would read: Account number: 12345 Payment Due Date: April 1 Amount Due: $2050.00 If payment is received after 4/15, $50 late fee will be charged. This is misleading about when payments were due, and what is necessary to avoid a late fee: • This indicates that the entire amount is due April 1. However, $1000 of that amount was due on March 1, and $50 was due March 16. • It also indicates that a late fee will be charged if the borrower does not pay $2050. In fact, there would be a late fee only if the borrower does not pay $2000. There is a concern that servicers could be sued under UDAP and UDAAP laws for displaying information in this misleading manner. The H-30(B) model form suggests that the coupon on the statement should reflect $2050. Many servicers list the amount of PITI and late fees on their statement as the total amounts owed by the customer on the loan, but on the coupon list only the contractual amount that is due for the next month to avoid a late fee.	If there are past due amounts, they will need additional explanation. The Explanation of Amount due contains the necessary detail. If the CFPB will continue to require disclosure of the total amount due in addition to past due amounts in the first grouping, we make two recommendations: • Servicers should be permitted flexibility to also disclose that the amount is the total amount due at differing due dates, and that the payment required to avoid a late fee may differ from what is disclosed in this grouping. • Servicers who comply with the regulation should *per se* be deemed not to have committed a UDAP or a UDAAP.
131. Explanation of amount due for borrowers in bankruptcy or foreclosure or after maturity, § 41(d)(2)	Section 41(d)(2) requires disclosure of: "The following items, grouped together in close proximity to each other and located on the first page of the statement: (i) The monthly payment amount, including a breakdown showing	We request guidance on how the disclosure should be prepared. There is no monthly payment amount after acceleration or maturity. There may not be any amount due in a bankruptcy. We request clarification that in disclosing the amount due for Chapter

TOPIC	ISSUE	RECOMMENDATION
	how much, if any, will be applied to principal, interest, and escrow and, if a mortgage loan has multiple payment options, a breakdown of each of the payment options along with information on whether the principal balance will increase, decrease, or stay the same for each option listed; (ii) The total sum of any fees or charges imposed since the last statement; and (iii) Any payment amount past due." For borrowers in bankruptcy or foreclosure, it is unclear what this disclosure must contain.	13 borrowers under §§ 41(d)(1) and (2), it is permissible to use either: • The amounts due under the bankruptcy plan; or • The post petition amount. Also in disclosing the past payment breakdown under § 41(d)(3), the breakdown would be based on the contractual terms for Chapter 7 cases. For Chapter 13 cases, the servicer must have the flexibility to reflect pre- and post-petition amounts, and any other special payment received pursuant to court requirements.
132. Disclosure of fees, § 41(d)(2)(ii) and (d)(4)	Section 41(d)(2)(ii) requires disclosure of: "The total sum of any fees or charges imposed since the last statement[.]" Section 41(d)(4) requires disclosure of: "A list of all the transaction activity that occurred since the last statement. For purposes of this paragraph (d)(4), *transaction activity* means any activity that causes a credit or debit to the amount currently due. This list must include the date of the transaction, a brief description of the transaction, and the amount of the transaction for each activity on the list." Comment 41(d)(4)-1.iii provides that the disclosure should include: "The imposition of any fees (for example late fees)[.]"	We request clarification of the extent to which fees may be aggregated, as under § 41(d)(2)(ii) and perhaps comment 41(d)(4)-1.iii, or must be itemized, as under § 41(d)(4). We request clarification that identifying the fee as property preservation is sufficient, and that multiple similar charges may be aggregated. Some fees may need to be entered manually, sl flexibility is helpful. We request clarification that the fees charged since the last statement does not include fees for services rendered but for which the amount is not yet known and for which the account has not yet been charged. We request confirmation that amounts included in the regular monthly payment, *e.g.*, private mortgage insurance that is part of the escrow payment, and optional product payments, need not be separately disclosed as fees or charges on the Transaction Activity required under § 41(d)(4).

220

TOPIC	ISSUE	RECOMMENDATION
		We request clarification that multiple payments can be combined in showing the amount of a single activity. For example, if the monthly contractual payment is $1000 ($700 interest, $100 principal, and $200 escrow) and the borrower paid $1000 each on March 5 and 10, the next statement could show principal of $200, interest of $1400, and escrow of $400 in the Past Payments Breakdown. In the Transaction Activity section, the same statement would show "3/5/13 Payment Received - Thank You $1000" and "3/10/13 Payment Received – Thank You $1000" so that each payment would not need to be broken down separately.
133. What must be done to apply suspended funds, § 41(d)(5)	Section 41(d)(5) provides that periodic statements disclosures include: "If a statement reflects a partial payment that was placed in a suspense or unapplied funds account, information explaining what must be done for the funds to be applied." This plainly requires disclosure of what the borrower must do to have the funds applied to a full payment. Section 51.18 of the Freddie Mac guide permits applying a payment that is within $50 of the contractual amount, even if it is less than a full payment, by reducing the amount applied to the escrow balance.	We request clarification that a narrative statement (*e.g.* "when a contractual payment is received") or a total dollar amount can be used rather than requiring an actual itemization of how the funds would be applied to principal, interest, and escrow. We request confirmation that if a servicer applies a partial payment that is within $50 of the contractual payment, the servicer may show the shortage amount as part of the amount due, and may show the actual application in the past payment breakdown and transaction activity.
134. Definition of page, § 41(d)(5), (d)(8)	Section 41(d)(5) provides: "The information must be on the front page of the statement or, alternatively, may be included on a separate page enclosed with the periodic statement or in a separate letter."	We recommend that the reverse side of a piece of paper be deemed a "separate page" for these purposes. We request clarification of the definition of "page" and "first page" in electronic statements. It would be preferable not to define the term and to instead permit the servicer to include all information an any

TOPIC	ISSUE	RECOMMENDATION
	Section (d)(8)has similar language.	reasonable location, consistent with the clear and conspicuous requirements of § 1026.17(a)(1).
135. Delinquency information on a separate page, § 41(d)(8)	Section 41(d)(8) provides that delinquency information may be provided "on a separate page enclosed with the periodic statement or in a separate letter[.]"	We request clarification that such disclosures in a separate letter may be sent before the periodic statement is sent. For example, assume a borrower sends a partial payment on the 5th of the month but the servicer sends periodic statements after the courtesy period. Could this servicer send the partial payment disclosure promptly after receiving the partial payment? As this notice acknowledges receipt of the partial payment and informs the borrower what is necessary for the funds to be applied, this notice may prevent a default, and should be permissible before delivering the periodic statement.
136. Definition of delinquency, § 41(d)(8)	We suggest above, under Regulation X, Exceptions to the definition of loss mitigation option, § 31, some workout arrangements that are technically defaults, but for which the servicer agrees not to pursue its normal collection activities, in exchange for a borrower's agreement to make payments as agreed with the servicer.	These should be exceptions to the definition of delinquency under § 41(d)(8). The requirements for disclosing delinquency information in a periodic statement should be inapplicable, as discussed above.
137. Date of delinquency, § 41(d)(8)(i)	Section 42(d)(8)(i) provides that periodic statements disclosures include the date the consumer became delinquent.	We request clarification of whether this includes or ignores any grace period. If a payment is due on the 1st and there is no late fee until the 16th, what is the date of delinquency?
138. Notification of possible delinquency expenses, § 41(d)(8)(ii)	Section 41(d)(8)(ii) requires delinquency information to include: "A notification of possible risks, such as foreclosure, and expenses, that may be incurred if the delinquency is not cured[.]"	We request clarification that this requires a general mention of possible expenses rather than a breakdown of individual potential expenses.
139. Amount needed to bring the loan current,	Section 41(d)(8)(vi) requires disclosure of:	We request clarification of whether the "amount needed to bring the account current" is the amount of the next scheduled payment, whether

TOPIC	ISSUE	RECOMMENDATION
§ 41(d)(8)(vi)	"The total payment amount needed to bring the account current[.]" This is not a defined term.	it includes any unpaid late fees for prior late payments, and whether it is synonymous with all amounts due on the loan.
140. Periodic statement exemptions, § 41(e)	Periodic statements are not required for reverse loans, timeshare plans, and when coupon books are permitted. However, they are required while a loan is in a trial payment plan, and after it is accelerated or has matured. The model forms simply are not designed for these situations. The required information includes the monthly payment amount, under § 41(d)(2)(i). • What is the monthly payment amount during a trial payment period? • Disclosing the monthly payment after acceleration could strongly imply that the loan has not been accelerated. There is no monthly periodic payment after acceleration or maturity. Telling borrowers otherwise would be a serious disservice. The required information includes all activity since the last statement, under §41(d)(4). For a defaulted loan, this could amount to reinstatement amounts provided on a monthly basis. The benefits of such a disclosure are outweighed by the costs of producing them. The rule does not address the point in the foreclosure process after which periodic statements are no longer required.	There should be no requirement for periodic statements after a loan is accelerated or has matured because the model form does not accommodate these circumstances. The CFPB should not require periodic statements after a loan is referred to foreclosure. Servicing personnel assigned to a borrower are required to provide all information a borrower requests, so additional disclosures, especially disclosures that could be misleading, should not be required. If the CFPB will require periodic statements after a borrower is referred to foreclosure, we recommend model language and examples. We recommend model language and examples of completed model forms for loans in a trial payment plan. A trial payment period is actually a delinquent loan even if the borrower is making the trial payments. At a minimum, the CFPB should make clear that providing a required periodic statement during a trial payment plan or after acceleration is under no circumstances a UDAP or UDAAP.
141. Coupon books for daily simple interest loans with a fixed rate, § 41(e)(3)	Coupon books, rather than periodic statements, are permissible for fixed-rate loans if a servicer provides certain information.	We request clarification of whether coupon books are permissible for daily simple interest loans that have a fixed rate.
142. Updated coupon		We request clarification of whether coupon books are permissible for

223

TOPIC	ISSUE	RECOMMENDATION
books for ARM loans§ 41(e)(3)		ARM loans if the servicer updates the coupon book with each payment change, and includes the information specified in § 41(e)(3)
143. Fixed-rate, non-escrowed loans paid by ACH, § 41(e)(3)		We request clarification of whether a servicer may send neither a coupon book nor periodic statements to borrowers who have a fixed-rate, non-escrowed loan that is not 45 days delinquent, and who pay by ACH. These borrowers have agreed to pay by ACH, and the payments do not adjust, so there appears no reason to send periodic statements or coupon books.
144. Small servicer exemption for seller-financed loans, § 41(e)(4)	A consumer may sell a home and provide financing to the buyer. The seller may ask a bank to process regular payments, with an agreement that the bank is responsible solely for collecting regularly scheduled payments and that it has no responsibilities if the loan becomes delinquent.	We request clarification of whether, in this case, assuming the loan is a federally-related mortgage loan, the bank must include this loan in counting the number of loans it services for purposes of the small servicer exemption.
145. Temporarily servicing loans subject to a forward commitment at origination, § 41(e)(4)(ii)(A)	The small servicer exemption applies to servicers that service no more than 5000 loans. Small servicers commonly originate loans, with a commitment at origination to sell the loan and release the servicing, although the secondary market transfer may not take place simultaneously (typically it occurs in 30 days or less).	We request clarification that a loan that the servicer will not service does not count towards the 5000 loan small servicer definition.
146. Definition of small servicer's affiliate, § 41(e)(4)(iii)	The small servicer exemption depends on the number of loans serviced by a servicer and its affiliates.	We request clarification that the § 1026.32(a)(2) definition of affiliate applies for the small servicer exemption in both Regulation X and Regulation Y. This definition provides: "*Affiliate* means any company that controls, is controlled by, or is under common control with another company, as set forth in the Bank Holding Company Act of 1956[.]"

CONSUMER MORTGAGE COALITION

GUIDANCE REQUESTS for MORTGAGE ORIGINATION REGULATIONS to the BUREAU OF CONSUMER FINANCIAL PROTECTION

Working Document
June 3, 2013

225

HIGHEST PRIORITY

MEDIUM PRIORITY

HIGHEST PRIORITY

TOPIC	PROVISION	RECOMMENDATION
Ability to Repay Regulation		
1. Self-employed consumers	Appendix Q § I.D.4.c requires self-employed consumers to provide: "Year to date profit and loss (P&L) statement and balance sheet[.]"	We request clarification that this permits creditors to rely on documents that the consumer or the consumer's company generates, and that audited financial statements are not required.
2. Planned retirement	Comment 43(c)(1)-2 provides: "A change in the consumer's circumstances after consummation (for example, a significant reduction in income due to a job loss or a significant obligation arising from a major medical expense) that cannot be reasonably anticipated from the consumer's application or the records used to determine repayment ability is not relevant to determining a creditor's compliance with the rule. However, if the application or records considered at or before consummation indicate there will be a change in a consumer's repayment ability after consummation (for example, if a consumer's application states that the consumer plans to retire within 12 months without obtaining new employment or that the consumer will transition from full-time to part-time employment), the creditor must consider that information under the rule." Appendix Q § I.B.i note I provides: "Effective income for consumers planning to retire during the first three-year period must include the amount of: a. Documented retirement benefits; b. Social Security payments; or c. Other payments expected to be received in retirement.	Comment 43(c)(1)-2 gives the required consideration only for a consumer who states a plan to retire within 12 months, and the appendix gives the required documentation only for consumers who plan to retire in three years. Neither states what is required in other circumstances. Is retirement only relevant if a consumer plans to retire in 12 months or 3 years? If not, what is required in the case of a consumer who states a plan to retire in 4, 5, 10, or 20 years, or who does not have a planned retirement date? How definite must a future possible income reduction be before a creditor must consider it? Do the answers to these questions differ under § 43(c) and appendix Q?
3. Calculation of loan	Loan payment amounts and DTI are calculated differently depending on	Creditors that make an intended QM loan that due to error is not a QM

TOPIC	PROVISION	RECOMMENDATION
payment and DTI	which standard the creditor uses. <u>General repayment ability (non-QM)</u> • For loans with no balloon, IO period, or negative amortization, creditors must calculate the loan payment using the greater of the introductory rate or the fully-indexed rate. § 43(c)(5)(i). • If creditors calculate DTI, they must use the payments on: the covered transaction; simultaneous loans; mortgage-related obligations; and current debt obligations, alimony, and child support. § 43(c)(7). <u>General QM definition</u> • Under the general QM definition, the loan payment is based on the maximum rate during the first five years. § 43(e)(2)(iv)(A). • The required 43 percent DTI is determined using the payments on the covered transaction; simultaneous loans; and mortgage-related obligations. § 43(e)(2)(iv). <u>Special agency QM definition</u> • The agencies also have standards. Fannie Mae, for example, bases loan payment calculations on an ARM loan using the greater of the note rate plus 2% or the fully-indexed rate, but using the note rate if it is fixed for longer than five years. Fannie Mae Selling Guide § B3-6-04. • Fannie Mae bases DTI calculations on monthly payments on installment debts that extend beyond ten months, and sometimes debts that do not extend ten months, plus alimony, child support, or maintenance payments that extend beyond ten months. Fannie Mae Selling Guide § B3-6-02.	loan will try to show compliance with the general repayment ability requirements. To do so, would a creditor need to establish the payment amount, DTI, and residual income calculated under the general repayment ability standards? At a minimum, if the creditor has information that shows a higher payment amount, lower DTI, and higher residual income than required under the non-QM standard, the creditor should be able to use that information to show compliance.

HIGHEST PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	Points and Fees	
4. Both an affiliate and a nonaffiliate may provide services	Points and fees include 4(c)(7) charges paid to service providers that are affiliated with the creditor, but exclude similar fees paid to a nonaffiliate. § 32(b)(1)(iii).	An affiliate may collect a fee and retain a nonaffiliate to perform a service. For example, a creditor may pay a fee to an affiliated title insurance agent who conducts a title examination, and who also pays part of the fee to an unaffiliated title insurer for insurance. We request confirmation that charges paid to affiliates are limited to amounts the affiliate retains. • This should be the case even if the combined charge is originally paid to the affiliate. • This should be the case regardless of whether the amount is disclosed to the consumer because the points and fees calculation is not required to be disclosed.
5. Financed points and fees and total loan amount	Section 32(b)(4) defines the total loan amount as depending on whether certain points and fees are financed: "The total loan amount for a closed-end credit transaction is calculated by taking the amount financed, as determined according to § 1026.18(b), and deducting any cost listed in § 1026.32(b)(1)(iii), (iv), or (vi) that is both included as points and fees under § 1026.32(b)(1) and financed by the creditor."	If the consumer prepays some but not all closing costs, or some but not all are paid from loan proceeds, how does the creditor determine which fees are financed and which the consumer paid?
6. Treatment of finance charge exclusions	The definition of points and fees includes several items that are defined as finance cbarge items under §§ 4(a) and 4(b). Points and fees also include additional items, in §§ 32(b)(1)(ii) – (vi) and (b)(2)(ii) – (viii). However, the points and fees definition does not expressly address items excluded from the finance charge definition under § 4(c) – (e).	We request clarification that items excluded from the finance charge under § 4(c) – (e) are not included in points and fees unless they are included in points and fees in §§ 32(b)(1)(ii) – (vi) or (b)(2)(ii) – (viii).
7. Discount points tied to non-LLPA risk factors	The section-by-section analysis for the ability-to-repay rule states: "To the extent that creditors offer consumers the opportunity to pay points to lower the interest rate that the creditor would otherwise	We request clarification that, aside from LLPAs, when a creditor offers a consumer the opportunity pay points to buy down a rate the creditor would otherwise charge to compensate for additional risk factors, the points are *bona fide* discount points if they otherwise satisfy the

232

TOPIC	PROVISION	RECOMMENDATION
	charge to recover the lost revenue from the LLPAs, such points may, if they satisfy the requirements of § 1026.32(b)(1)(i)(E) or (F), be excluded from points and fees as bona fide discount points." 78 Fed. Reg. at 6408, 6430 (Jan. 30, 2013).	requirements of § 1026.32(b)(1)(i)(E) or (F).
8. Definition of interest rate without any discount points	Section 32(b)(1)(i)(E) and (F) exclude *bona fide* discount points "if the interest rate without any discount does not exceed" specified levels.	We request confirmation that creditors are not required to offer a loan with exactly zero discount points as a prerequisite to excluding discount points from points and fees. We request clarity about identifying the undiscounted rate. A creditor could compensate for risk factors on a loan by charging points, by increasing the rate, or by a combination of the two. A creditor may not offer a rate with exactly zero discount points. For example, a creditor might offer a consumer the following options: • A rate of 4.000% with a credit to the borrower of .25 points; • A rate of 3.875% with the borrower paying .25 points; and • A rate of 3.750% with the borrower paying .75 points. In this example, which rate is the interest rate without any discount?
9. The interest rate compared to the APOR	Section 32(b)(1)(i)(E) and (F) exclude *bona fide* discount points "if the interest rate without any discount does not exceed" specified levels.	We request confirmation that the "interest rate" is the interest rate and not the APR. We request clarification of the interest rate on an ARM loan and step-rate loan.
10. Sufficient rate reduction to exclude discount points	Section 32(b)(3)(i) provides: "The term *bona fide discount point* means an amount equal to 1 percent of the loan amount paid by the consumer that reduces the interest rate or time-price differential applicable to the transaction based on a calculation that is consistent with established industry	On ARM loans, it is a common industry practice for discount points to buy down the introductory rate. We request conformation that discount points that buy down the introductory rate on an ARM loan rather than the rate after recast are "consistent with established industry practices for determining the amount of reduction in the interest rate" within the meaning of § 32(b)(3)(i) and (ii).

TOPIC	PROVISION	RECOMMENDATION
	practices for determining the amount of reduction in the interest rate or time-price differential appropriate for the amount of discount points paid by the consumer." Section 32(b)(3)(ii) uses very similar language.	
11. Points and fees paid by an employer	Current § 32(a)(1)(ii) defines points and fees to include amounts "payable by the consumer at or before loan closing[.]" As revised in the HOEPA rulemaking, this provision refers to the points and fees definition in § 32(b)(1) and (2) in the ability-to-repay rule. This definition includes points and fees "known at or before consummation" without regard to who pays them.	Limiting points and fees to those known at or before consummation is helpful because QM, QRM, and HOEPA status must be known before consummation. We suggest points and fees should also be limited to amounts the consumer actually pays. We request clarification that if a creditor pays an amount, or fails to charge it to the consumer, the amount is not included in points and fees. In a corporate relocation loan, an employer may pay points or fees on an employee's mortgage loan. • We request confirmation that employer-paid points and fees are excluded from the finance charge and from points and fees because they are an expense to the employer and a benefit to the consumer. • We request confirmation that if employer-paid points are included in the finance charge, they can be excluded from points and fees as *bona fide* discount points even though they are not directly "paid by the consumer" under § 43(b)(1)(i)(E) and (F), if they meet the applicable requirements. We also request confirmation that amounts paid by a property seller, or by a third party who provides closing cost assistance, are likewise excluded.

TOPIC	PROVISION	RECOMMENDATION
	QM Eligibility	
12. Creditor-paid principal curtailments	Section 43(e)(2)(i) provides that a loan qualifies as a QM loan if, among other things, it: "provides for regular periodic payments that are substantially equal, except for the effect that any interest rate change after consummation has on the payment in the case of an adjustable-rate or step-rate mortgage[.]"	Some flexibility is warranted for loans that help consumers pay down the principal. A creditor may offer a loan on which the creditor provides principal curtailments tied to the amount of deposits the consumer has with the creditor. These curtailments reduce the principal balance and shorten the loan term, but do not alter the monthly payment. We request confirmation that this curtailment benefit does not disqualify a loan from QM eligibility.
13. Agency standards unrelated to ability to repay – representations and warrants; jumbo loans	Proposed comment 43(e)(4)-4 provides that a loan that meets the special agency QM definition does not need to meet agency standards unrelated to repayment ability: "However, the creditor need not satisfy standards that are wholly unrelated to assessing a consumer's ability to repay that the creditor is required to perform such as requirements related to selling, securitizing, or delivering already consummated loans and any requirement that the creditor must perform after the consummated loan is sold, guaranteed, or endorsed for insurance such as document custody, quality control, or servicing."	We support this proposal. It can be difficult to separate requirements that address only the consumer's ability to repay from underwriting requirements that include other risk factors. The GSEs and agencies generally require representations and warrants that a loan has been originated in compliance with all applicable law. We request confirmation that such representations and warrants, themselves, are not underwriting requirements, and therefore noncompliance with representations or warrants is irrelevant to QM status. We request confirmation that agency standards related to the amount of loan principal are not related to repayment ability and that loans with a principal amount greater than the agency standards are eligible for the special agency QM definition.
14. Agency standards in written agreements	Proposed comment 43(e)(4)-4.1 provides that a loan can be a QM if: "The loan conforms to the relevant standards set forth in the Fannie Mae Single-Family Selling Guide or the Freddie Mac Single-Family Seller/Servicer Guide in effect at the time, or to standards set forth in a written agreement between the creditor and Fannie Mae or Freddie	We request confirmation that: • If a correspondent lender makes a loan that has a variance from agency standards, that loan is eligible for special agency QM status if the correspondent sells the loan to a creditor who has a written agreement with Fannie Mae or Freddie Mac reflecting that variance. • Errors and defects that fall within an agency's tolerances, or for

TOPIC	PROVISION	RECOMMENDATION
	Mac that permits variation from the standards of those guides[.]"	which there is a written agreement or understanding that the loans will not be subject to repurchase or indemnification demands, are eligible for and retain special agency QM status. • A loan for which a creditor cures errors after consummation, in accordance with GSE and agency standards, retains special agency QM status.
15. Agency standards change after consummation	Proposed comment 43(e)(4)-5 provides: "[E]ach loan should be evaluated by the creditor based on the facts and circumstances relating to the eligibility of that loan at the time of consummation." The comment gives two examples of DU input errors that are discovered after consummation.	This comment appears to assume that it is possible to know whether the DU recommendation would have changed if accurate information had been input. While DU and LP have processes for re-running loans, they do not always allow for re-running the loan using the same version of DU or LP or the same credit report used to originate the loan. We recommend that the CFPB work with the GSEs to allow creditors to re-run DU and LP with the same AUS version and the same credit report. Barring that, if the credit report or DU or LP has changed, will a DU or LP recommendation be evidence of compliance or noncompliance?

16. Assumptions	Comment 43(a)-1 provides:
	"In general, § 1026.43 applies to consumer credit transactions secured by a dwelling. . . . In addition, § 1026.43 does not apply to any change to an existing loan that is not treated as a refinancing under § 1026.20(a)."
	It is unclear whether assumptions are subject to the rule. An assumption involves a change to an "existing loan" but the requirements to provide disclosures on assumptions are in § 20(b), while § 20(a) requires disclosures for refinancings.
		We recommend that § 43 not apply to assumptions. If it does, we request confirmation of the following:
		• If an assumed loan is held in portfolio, it can qualify for QM status under the special agency QM definition.
		• The rule does not apply to a loan originated before the regulation's effective date and assumed after that effective date.
		• If an assumable ARM loan is a QM, the regulation will not apply to a subsequent assumption of that loan. Otherwise:
		  o What is the introductory rate under § 43(c)(5)(i)?
		  o What is the "maximum interest rate that may apply during the first five years after the date on which the first regular periodic payment will be due" in § 43(e)(2)(iv)(A)?

	Residual Income	
17. Need for a residual	The section-by-section analysis states:	Creditors need substantially more certainty before the effective date of

TOPIC	PROVISION	RECOMMENDATION
income test	"[T]he Bureau believes that providing broad standards for the definition and calculation of residual income will help preserve flexibility if creditors wish to develop and refine more nuanced residual income standards in the future. The Bureau accordingly does not find it necessary or appropriate to specify a detailed methodology in the final rule for consideration of residual income." * * * "The Bureau expects to study residual income further in preparation for the five-year review of this rule required by the Dodd-Frank Act." 78 Fed. Reg. at 6487 and 6528 (Jan. 30, 2013).	the regulation on how to define and calculate residual income and what level of residual income is sufficient. We strongly urge the CFPB not to wait years before establishing residual income standards. We instead recommend permitting use of the VA residual income test, at least until the CFPB creates a replacement test.
18. Identifying and quantifying items relevant to residual income, and determining what residual income is sufficient	Comment 43(c)(1)-1.ii.B.5 provides that evidence that a creditor's ability-to-repay determination was not reasonable or in good faith may include: "The creditor disregarded evidence that the consumer may have insufficient residual income to cover other recurring obligations and expenses, taking into account the consumer's assets other than the property securing the loan, after paying his or her monthly payments for the covered transaction, any simultaneous loans, mortgage-related obligations, and any current debt obligations[.]" In addition, to make non-QM loans under § 43(c), creditors are required to consider either residual income or DTI, but neither is specified. To make higher-priced QM under § 43(e)(1)(ii)(B), creditors must be able to determine:	Both §§ 43(c) and 43(e) use a residual income concept, but the regulation and commentary do not set any standard. Clarity is needed in identifying which items are and are not relevant to residual income, how to quantify the relevant items, whether the household is relevant or only the applicant, and in determining how much residual income is or is not sufficient. Further, it is not clear whether the same standards apply under §§ 43(c) and 43(e). <u>Identifying what is relevant to residual income</u> It is quite unclear what is included in and excluded from residual income. • Under § 43(c), what expenses, other than those enumerated in § 43(c)(2)(i) through (vi), are relevant to residual income? • Does the characterization of these fees as "obligations" in comment 43(c)(1)-1.ii.B.5 mean to exclude amounts spent on food, clothing, and gasoline because they are largely discretionary? What is the

TOPIC	PROVISION	RECOMMENDATION
	"that the consumer's income, debt obligations, alimony, **child support**, and the consumer's monthly payment (including mortgage-related obligations) on the covered transaction and on any simultaneous loans of which the creditor was aware at consummation would leave the consumer with **insufficient residual income or assets** other than the value of the dwelling (including any real property attached to the dwelling) that secures the loan with which to meet **living expenses**, including any **recurring and material non-debt obligations** of which the creditor was aware at the time of consummation." The regulation and commentary do not define the terms above in bold. Comment 43(e)(1)(ii)-1 provides: "For example, a consumer may rebut the presumption with evidence demonstrating that the consumer's residual income was insufficient to meet living expenses, such as food, clothing, gasoline, and health care, including the payment of recurring medical expenses of which the creditor was aware at the time of consummation . . . ."	comparable standard under § 43(e)? • Under § 43(e)(1)(ii)(B), what are living expenses, and recurring and material non-debt obligations? • Is discretionary spending relevant? • If one borrower pays a recurring child care bill while another borrower does not, is child care a recurring obligation for either borrower? • To what extent are child care expenses, medical costs, food costs, utilities, transportation costs, or federal, state and local income taxes included or excluded? <u>Quantifying the amounts for residual income items</u> • On what basis is the creditor is to determine the amounts of the relevant residual income items? • Can creditors rely on information provided by the consumer? • What if the consumer does not track the relevant items? • To what extent can creditors rely on average amounts instead of having to obtain customer-specific information? • Do utility bills vary by geography? • Do the relevant costs include actual costs even if part of the actual cost is discretionary? • If a consumer informs a creditor about non-debt obligations or expenses, must the creditor document and verify them? <u>Consumer or household?</u> It appears under § 43(c) and 43(e) that residual income is computed solely using the consumer's information. • Should creditors consider only the information of applicants? • If the transaction is subject to the right to cancel so that an owner

TOPIC	PROVISION	RECOMMENDATION
		who is not a borrower is defined as a "consumer" under § 2(a)(11), must or may that individual's information also be considered? • Should creditors consider information of other household members who are neither borrowers nor owners? • May creditors consider "income and assets to which the consumer has a reasonable expectation of access" as under the <u>recently finalized</u> Card Act standard, 12 C.F.R. § 1026.51(a)(1)(ii)? <u>What amount of residual income is sufficient?</u> How are creditors and consumers to determine whether residual income is sufficient with neither numerical guidelines nor concrete guidance on the factors that creditors must consider? For each of these questions, an answer is needed under both § 43(c) and § 43(e). Substantially more clarity is needed before the regulation becomes effective.
19. Living expenses	Comment 43(c)(1)-1.ii.B.*5* provides that evidence that a creditor's ability-to-repay determination was not reasonable or in good faith may include: "The creditor disregarded evidence that the consumer may have insufficient residual income to cover other **recurring obligations and expenses**, taking into account the consumer's assets other than the property securing the loan, after paying his or her monthly payments for the covered transaction, any simultaneous loans, mortgage-related obligations, and any current debt obligations[.]"	Do recurring obligations and expenses in comment 43(c)(1)-1.ii.B.*5* differ from necessities in comment 43(c)(1)-1.ii.C?

TOPIC	PROVISION	RECOMMENDATION
	Comment 43(c)(1)-1.ii.C provides: "[A]n ability-to-repay determination may be unreasonable or not in good faith even though the consumer made timely payments for a significant period of time if, for example, the consumer was able to make those payments only by foregoing **necessities** such as food and heat."	
20. Basis for determination	Comment 43(c)(2)-1 provides: "A creditor may, but is not required to, look to guidance issued by entities such as the Federal Housing Administration, the U.S. Department of Veterans Affairs, the U.S. Department of Agriculture, or Fannie Mae or Freddie Mac while operating under the conservatorship of the Federal Housing Finance Agency."	We request confirmation that reliance on agency and GSE guidance, or on appendix Q, is *per se* compliance with § 43. We also request confirmation that a creditor that relies on the VA residual income standards, even for non-VA loans, cannot later be found to have "disregarded evidence that the consumer may have insufficient residual income" within the meaning of comment 43(c)(1)-1.ii.B.5; and cannot be found to have left the consumer with insufficient residual income or assets with which to meet living expenses andrecurring and material non-debt obligations under § 43(e)(1)(ii)(B).
21. Consistence with ECOA and FCRA	Comment 43(c)(1)-2 provides: "A change in the consumer's circumstances after consummation (for example, a significant reduction in income due to a job loss or a significant obligation arising from a major medical expense) that cannot be reasonably anticipated from the consumer's application or the records used to determine repayment ability is not relevant to determining a creditor's compliance with the rule. However, if the application or records considered at or before consummation indicate there will be a change in a consumer's repayment ability after consummation (for example, if a consumer's application states that the consumer plans to retire within 12 months without obtaining new employment or that the consumer will transition from full-time	To the extent that a creditor may need to ask about planned retirements, health care expenses, child care expenses, income and obligations of household members including a spouse, and medical information, the requirements could conflict with ECOA and FCRA requirements. Section 43(c)(2)(vi) requires consideration of a consumer's "child support[.]" Not requiring or permitting a creditor to ask a consumer who is expecting a child about future child support is insufficient to remove the conflict of laws because it does not address whether the information the creditor may not request is relevant to ability-to-repay determinations. We request more guidance about how creditors can request and evaluate information as required or permitted under § 43 without violating either

240

TOPIC	PROVISION	RECOMMENDATION
	to part-time employment), the creditor must consider that information under the rule." Comment 43(c)(1)-3 provides: "Section 1026.43(c)(1) does not require or permit the creditor to make inquiries or verifications prohibited by Regulation B, 12 CFR part 1002."	ECOA or FCRA.
Loan Originator Compensation Regulation		
22. Assisting a consumer	Comment 36(a)-1.i.A.*3* provides that a loan originator includes a person who: "Assist[s] a consumer in obtaining or applying for consumer credit by advising on specific credit terms (including rates, fees, and other costs)[.]" Section 36(a)(1) defines a loan originator as a person who for compensation: "[T]akes an application, offers, arranges, assists a consumer in obtaining or applying to obtain, negotiates, or otherwise obtains or makes an extension of consumer credit for another person; or through advertising or other means of communication represents to the public that such person can or will perform any of these activities." Regulation G § 1007.102 defines a mortgage loan originator as an individual who:	We request confirmation that a person who provides publicly available loan rates, and who is not thereby a mortgage loan originator under Regulation G, is not thereby also a loan originator under Regulation Z.

TOPIC	PROVISION	RECOMMENDATION
	"(i) Takes a residential mortgage loan application; and (ii) Offers or negotiates terms of a residential mortgage loan for compensation or gain."	
23. Bonus as proxy	Section 36(d)(1)(iv) permits compensation to a loan originator from a non-deferred profits-based compensation plan that is determined with reference to the profits of the person from mortgage-related business, if, among other things: • The compensation paid to an individual loan originator does not in the aggregate exceed 10 percent of the individual loan originator's total compensation corresponding to the time period for which the compensation plan is paid; or • The individual was a loan originator for ten or fewer transactions consummated during the 12-month period preceding the date of the compensation determination.	We request clarification that any such bonus is *per se* not a proxy for loan terms under § 36(d)(1). But if that compensation is a proxy, another question arises about senior executives and attorneys. Many creditors have bonus pools that include nonmortgage profits. A senior executive or attorney who is not a traditional loan originator occasionally steps in to resolve a customer complaint, which may include adjusting fees or rates on a mortgage loan application in process. Creditors do not necessarily track this participation. The senior executive or attorney may receive a bonus after stepping in on more than ten applications in a year, or may receive a bonus of more than ten percent of total compensation for the relevant period. We request confirmation that this tangential activity does not mean the compensation is prohibited. The senior executive or attorney in this case is not in a position to earn more compensation by steering the consumer to a worse loan. At the same time, the tangential assistance could taint an annual bonus, which would be disproportionate to any potential steering.
24. Referral to a loan originator	Comment 36(a)-1.i.A.*1* provides that a loan originator includes a person who: "Refer[s] a consumer to any person who participates in the origination process as a loan originator. Referring includes any oral or written action directed to a consumer that can affirmatively influence the consumer to select a particular loan originator or creditor to obtain an extension of credit when the consumer will pay	We request clarification that a employee of a creditor who need not register as a loan originator under Regulation G is not a loan originator under Regulation Z if that employee refers a consumer to another employee of the creditor. For example, assume that a bank teller is not a loan originator under Regulation G because the teller does not take, or have access to, application information and does not offer loan terms. A teller may be

242

TOPIC	PROVISION	RECOMMENDATION
	for such credit." Comment 36(a)–4.11.B provides that loan origination does not include persons who: "[P]rovide loan originator or creditor contact information in response to the consumer's request, provided that the employee does not discuss particular credit terms available from a creditor and does not refer the consumer, based on the employee's assessment of the consumer's financial characteristics, to a particular loan originator or creditor seeking to originate particular credit transactions to consumers with those financial characteristics[.]"	aware that a consumer is an existing mortgage customer of the bank. The teller may accept a payment on the mortgage loan, or, when the consumer conducts a transaction with the teller, the bank's system may alert the teller that the consumer has a mortgage with the bank at a rate that is likely higher than the current rate. In these circumstances, the teller may suggest that the consumer speak to the branch's registered loan originator about a possible refinance to a lower rate. If asked, the teller will quote tbe publically posted rates for refinances. If this conversation results in a closed loan, the teller will receive a small payment. This is an example of cross-selling, not steering. We request confirmation that this activity does not make the teller a loan originator under Regulation Z, thereby triggering the qualification requirements, the restrictions on permissible compensation, and does not result in including the payment in points and fees under § 32(b).
25. EEOC guidance against using credit reports and criminal histories	The EEOC provides guidance that inquiry into a job applicant's credit rating and similar information "generally should be avoided but that "[e]xceptions exist if the employer can show that such information is essential to the particular job in question." The EEOC also discourages employers from using arrest and conviction records as an absolute measure to prevent an individual from being hired except to the extent tbat it is evident that the applicant cannot be trusted to perform the duties of the position when considering the circumstances.	The impact of the EEOC guidance and prohibitions will vary depending on the definition of loan originator. For that reason, we are unsure of the prioritization of this issue. If every bank teller who cross-sells is a loan originator, the impact could be large. We are not sure the EEOC would take the position that one or a few relatively minor negative items on a credit report should disqualify a person from being a bank teller. Such a position could have a disparate impact on certain classes of job applicants. We therefore urge the CFPB not to define loan originator this broadly. Consultation with the EEOC may be beneficial. We request confirmation that the background checks required by § 36 are "essential to the particular job on question." We request

243

TOPIC	PROVISION	RECOMMENDATION
		confirmation that when § 36 prohibits employing a person because of a criminal history that this means "it is evident that the applicant cannot be trusted to perform the duties of the position" within the meaning of the EEOC's language.
	HOEPA Regulation	
26. HOEPA APR	The HOEPA regulation defines high-cost mortgages to include loans on which the APR exceeds the APOR by a specified spread. However, the APR used in this definition is not the same APR used for consumer disclosure purposes. Rather, it is: "(i) For a transaction in which the annual percentage rate will not vary during the term of the loan or credit plan, the interest rate in effect as of the date the interest rate for the transaction is set; (ii) For a transaction in which the interest rate may vary during the term of the loan or credit plan in accordance with an index, the interest rate that results from adding the maximum margin permitted at any time during the term of the loan or credit plan to the value of the index rate in effect as of the date the interest rate for the transaction is set, or the introductory interest rate, whichever is greater; and (iii) For a transaction in which the interest rate may or will vary during the term of the loan or credit plan, other than a transaction described in paragraph (a)(3)(ii) of this section, the maximum interest rate that may be imposed during the term of the loan or credit plan."	• For an ARM loan with mortgage insurance, should the mortgage insurance premiums and termination date reflect the same assumptions as are used for the disclosed APR or should they reflect the interest rate assumptions used for the HOEPA APR? • Should per diem interest included in the HOEPA APR calculation reflect the actual charge based on the initial interest rate, or when the fully-indexed rate is higher, should the per diem interest be inflated to reflect that higher fully-indexed rate?
27. Counseling disclosure requirements are needed	In Regulation X, § 1024.20(a)(1) finalized in the HOEPA rule, requires delivery of: "a clear and conspicuous written list of homeownership counseling	Creditors cannot begin to work on the systems requirements for producing this disclosure until the CFBP provides information on its content and format, the required data inputs to obtain information from the CFPB or HUD data, and instructions for how to use the information

HIGHEST PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	organizations that provide relevant counseling services in the loan applicant's location." The list must be provided from either: (i) The Web site maintained by the Bureau for lenders to use in complying with the requirements of this section; or (ii) Data made available by the Bureau or HUD for lenders to use in complying with the requirements of this section, provided that the data is used in accordance with instructions provided with the data."	obtained from the CFPB or HUD to create that disclosure. We request that the CFPB provide the necessary information as soon as possible. If it will be delayed, we request additional implementation time. To begin planning the implementation process, it is important to know whether the disclosure will differ for loans that require and do not require counseling.

245

MEDIUM PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	Ability to Repay	
28. Relevance of oral information	The section-by-section analysis provides: "[A] consumer may seek to show that a loan does not meet the requirements of a qualified mortgage by relying on information provided orally to the creditor or loan originator to establish that the debt-to-income ratio was miscalculated. Alternatively, a consumer may seek to show that the creditor should have known, based upon facts disclosed orally to the creditor or loan originator, that the consumer had insufficient residual income to be able to afford the mortgage. The final rule does not preclude the use of such oral evidence in ability-to-repay cases." 78 Fed. Reg. 6408, 6512 (January 30, 2013). Comment 43(c)(1)-2 provides: "[I]f the application or records considered at or before consummation indicate there will be a change in a consumer's repayment ability after consummation (for example, if a consumer's application states that the consumer plans to retire within 12 months without obtaining new employment or that the consumer will transition from full-time to part-time employment), the creditor must consider that information under the rule."	The comment appears to limit the creditor's required consideration to "the application or records[,]" which may be inconsistent with the section-by-section analysis. Or are there some types of orally volunteered information that the creditor must consider but other types of information that only need to be considered if they are written?
29. Credit history, DTI, and residual income	Comment 43(c)(2)(viii)-1 provides: "'Credit history' may include factors such as the number and age of credit lines, payment history, and any judgments, collections, or bankruptcies. . . . The rule also does not specify which aspects of	• For a non-QM loan, must there be some difference between DTI requirements, residual income requirements, or both, for applicants with good history compared to applicants with poor history to demonstrate that the creditor considered credit history? • Could a creditor's determination to approve a loan to an applicant

	credit history a creditor must consider or how various aspects of credit history should be weighed against each other or against other underwriting factors. Some aspects of a consumer's credit history, whether positive or negative, may not be directly indicative of the consumer's ability to repay. A creditor therefore may give various aspects of a consumer's credit history as much or as little weight as is appropriate to reach a reasonable, good faith determination of ability to repay." Comment 43(c)(7)-3 provides: "The creditor may consider factors in addition to the monthly debt-to-income ratio or residual income in assessing a consumer's repayment ability."	with a good credit score be appropriate if the DTI and/or residual income requirement were less strict, on the basis that credit history shows willingness to repay but not ability to repay? • Is it sufficient to consider credit history in determining whether to make the loan but not the DTI and/or residual income requirements?
30. Relevance of LTV to ability to repay	Comment 43(c)(1)-1.ii.A.*2* provides that evidence that a creditor's ability-to-repay determination was reasonable and in good faith includes: "The creditor used underwriting standards that have historically resulted in comparatively low rates of delinquency and default during adverse economic conditions[.]"	Neither the general ability to repay standard nor the QM standard require a creditor to consider the LTV. Loans with higher LTVs have higher delinquency rates during adverse economic conditions. If a creditor's underwriting standards do not treat high-LTV loans in a more conservative manner than low-LTV loans, is this evidence that the creditor's determination of ability to repay was not reasonable and in good faith?
31. Community lending exemption	Section 43(a)(12) defines simultaneous loan as: "another covered transaction or home equity line of credit subject to § 1026.40 that will be secured by the same dwelling and made to the same consumer at or before consummation of the covered transaction or, if to be made after consummation, will cover closing costs of the first covered transaction."	The May 2013 ability-to-repay amendments provide an exemption from the ability to repay requirement for certain creditors who typically make subordinate loans or forgivable grants for closing costs and down payment assistance. We request confirmation that the subordinate lien or forgivable grant would not be a "covered transaction" or a "simultaneous loan" that the senior creditor must consider for ability-to-repay purposes. • Otherwise, we request guidance on how the senior creditor should consider this simultaneous loan. The creditor may not be able to accurately determine the payment amount on these loans.

		• If the subordinate lien or forgivable grant is not a simultaneous loan, it is not clear how the senior creditor could verify the exemption. We suggest that the CFPB or HUD provide a website listing exempt entities. • We request guidance on how to verify the status of non-profits and whether they meet the requirements of the exemption.
	Affiliate Fees	
32. Exemptions from points and fees		We request confirmation that points and fees do not include items paid to a creditor's affiliate that are none of the following: • Finance charge items under § 4(a) or (b); • Section 4(c)(7) charges; • Insurance items listed in §§ 32(b)(1)(iv) or (b)(2(iv).
33. Creditor-paid affiliate fees	Comment 32(b)(1)(i)-1 provides: "In general, a charge or fee is 'known at or before consummation' if the creditor knows at or before consummation that the charge or fee will be imposed in connection with the transaction, even if the charge or fee is scheduled to be paid after consummation."	We request confirmation that if a creditor, rather than the consumer, pays a charge to an affiliate, the charge is not included in points and fees because it is not "imposed in connection with the transaction."
	QM Eligibility	
34. Payments from a subsidy account	Section 34(e)(2)(i) requires QM loans generally to have "regular periodic payments that are substantially equal[.]"	A loan may have substantially equal monthly payments, and a subsidy account, from which a contribution is made to the monthly loan payments for an initial period of time. We request clarification that these loans are eligible to be QM loans, regardless of whether the borrower or the borrower's employer funds the subsidy account.
35. Loan term for balloon and IO loans	Section 43(b)(6) defines the loan term as the period of time to repay the obligation in full. Comment 43(b)(6)-1 gives an example: "For example, a loan with an initial discounted rate that is fixed for the first two years, and that adjusts periodically for the next 28 years	For balloon and interest-only loans, is the loan term the "amortization period on which the periodic amortizing payments are based" or the "period of time to pay the obligation in full"?

	has a loan term of 30 years, which is the amortization period on which the periodic amortizing payments are based."	
36. Agency standards unrelated to ability to repay	Proposed comment 43(e)(4)-4 provides that a loan can maintain QM status under the special agency QM definition if: "the creditor [does] not satisfy standards that are wholly unrelated to assessing a consumer's ability to repay that the creditor is required to perform such as requirements related to selling, securitizing, or delivering already consummated loans and any requirement that the creditor must perform after the consummated loan is sold, guaranteed, or endorsed for insurance such as document custody, quality control, or servicing."	In some cases, it may be difficult to separate requirements that address only the consumer's ability to repay from underwriting requirements that include other risk factors. Meeting post-consummation requirements sometimes depends upon third parties, and a failure of third parties to meet these requirements should not cause the loss of QM status. For example, in escrow states, Fannie Mae requires a final HUD-1 signed by the settlement agent, but the creditor cannot ensure that the settlement agent provides it. Other examples include collecting follow-up documentation such as recording documents and work completion escrow documents. QM status needs to be known before consummation, so post-consummation requirements should be irrelevant to QM status. We request confirmation that failure to meet post-consummation requirements does not cause a loss of QM status, regardless of who caused the failure.
37. GSE written waivers	Proposed comment 43(e)(4)-4.i provides that a loan can maintain QM status under the special agency rule if it meets: "[S]tandards set forth in a written agreement between the creditor and Fannie Mae or Freddie Mac that permits variation from the standards of [the GSE selling] guides[.]"	We request confirmation that a GSE's written waiver of a requirement on an individual loan or group of loans would allow the loans or loans to retain QM status.
	Fair Lending	
38. Ability-to-repay and disparate impact		Will the CFPB, DOJ, or HUD bring disparate impact cases if creditors make only QM loans? If a creditor has a policy of making only QM loans but one or some loans are later deemed to be non-QM because of ambiguities in appendix Q, will that creditor be more susceptible to disparate impact liability? Guidance on how to reconcile the conflicting policy goals of ability-to-

		repay requirements and disparate impact would most helpful.
	Record Retention	
39. Record retention	Section 25(a) (in the QM rule) and 25(c)(2) (in the loan originator compensation rule) require: • Creditors to retain evidence of compliance with Regulation Z for two years; and • Creditors to "records sufficient to evidence all compensation" it pays to loan originators for three years. • Loan originator organizations to retain "records sufficient to evidence all compensation" it receives, or that it pays to an individual loan originator, for three years.	We request confirmation that this does not require each consumer mortgage creditor nationwide to retain records showing every GSE standard applicable to each loan, every DU and LP amendment, and all information input into DU or LP for every QM loan. We also request confirmation that it does not require retaining all information showing how interest rate reductions for discount points were determined.
	Loan Originator Compensation and Qualification	
40. Employees who change jobs but not employers	Comment 36(f)(3)(i)-3 provides: "Section 1026.36(f)(3)(i) does not require the loan originator organization to obtain the covered information for an individual whom the loan originator organization hired as a loan originator on or before January 10, 2014, and screened under applicable statutory or regulatory background standards in effect at the time of hire. However, if the individual subsequently ceases to be employed as a loan originator by that loan originator organization, and later resumes employment as a loan originator by that loan originator organization (or any other loan originator organization), the loan originator organization is subject to the requirements of § 1026.36(f)(3)(i)."	We request confirmation that this exemption also applies for an employee who ceases to be a loan originator but remains with the same employer, then returns to a loan originator position still with the same employer.

250

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	Points and Fees	
41. Hazard and credit property insurance	Section 32(b)(1)(i) includes in points and fees certain finance charge items. The finance charge definition excludes "any charge of a type payable in a comparable transaction." § 4(a). Hazard is a type of charge payable in a cash purchase, and should not be in points and fees. Section 32(b)(1)(iv) includes in points and fees (emphasis added): "**Premiums** or other charges payable at or before consummation **for any** credit life, credit disability, credit unemployment, or credit property insurance, or any other life, **accident**, health, or loss-of-income **insurance** for which the creditor is a beneficiary, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract[.]" Comment 32(b)(1)(iv) explains that credit property insurance does not include homeowners' insurance because homeowners' insurance covers the consumer's property interest. It also explains that accident insurance premiums are included on points and fees only if the consumer is not a beneficiary: "2. *Credit property insurance.* Credit property insurance includes insurance against loss of or damage to personal property, such as a houseboat or manufactured home. Credit property insurance covers the creditor's security interest in the property. Credit property insurance does not include homeowners' insurance, which, unlike	We request that the comment explicitly exclude from points and fees homeowner's insurance premiums paid at or before closing. This insurance covers the dwelling attached to real property, including a condominium or cooperative unit, and insures the borrower's interest, subject to the mortgage. Comment 32(b)(1)(iv) addresses these insurance premiums only indirectly. Consumers purchase homeowner's insurance in a comparable cash transaction so the premiums are excluded by § 4(a), yet are included in points and fees under comment 32(b)(1)(iv). Comment 32(b)(1)(iv) states that credit property insurance differs from homeowner's insurance, but does not make the distinction clear. Is the distinction that credit property insurance insures only the creditor's security interest, while hazard insurance insures the consumer, subject to the mortgage? If so, we request confirmation that the premiums paid at or before closing for required hazard and flood insurance to a nonaffiliate are not included in points and fees if the consumer is the insured and there is a loss payable mortgagee clause. Is credit property insurance limited to insurance on personal property such that any insurance on a real property dwelling is hazard insurance, and therefore not included in points and fees as long as it is excluded from the finance charge? Is credit property insurance in §§ 32(b)(1)(iv) and 32(b)(2)(iv) defined

TOPIC	PROVISION	RECOMMENDATION
	credit property insurance, typically covers not only the dwelling but its contents and protects the consumer's interest in the property. 3. *Life, accident, health, or loss-of-income insurance.* Premiums or other charges for these types of insurance are included in points and fees only if the creditor is a beneficiary. If the consumer or another person designated by the consumer is the sole beneficiary, then the premiums or other charges are not included in points and fees."	the same way as in § 36(i)(2)(i) (which prohibits financing single premium credit insurance)? It is not always clear under state law whether a cooperative is real or personal property. Is insurance required on a cooperative credit property insurance or hazard insurance? Is flood insurance credit property insurance or hazard insurance?
	Ability to Repay	
42. Underwriting standards based on empirical information	Comment 43(c)(1)-1.i is intended to permit creditors to select and amend their underwriting requirements: "Section 1026.43(c) and the accompanying commentary describe certain requirements for making this ability-to-repay determination, but do not provide comprehensive underwriting standards to which creditors must adhere. For example, the rule and commentary do not specify how much income is needed to support a particular level of debt or how credit history should be weighed against other factors. So long as creditors consider the factors set forth in § 1026.43(c)(2) according to the requirements of § 1026.43(c), creditors are permitted to develop their own underwriting standards and make changes to those standards over time in response to empirical information and changing economic and other conditions."	Underwriting is in part a matter of judgment. There is a large body of underwriting studies, the extent to which they are empirical is debatable, and they often conflict. This comment could result in litigation over which empirical information a creditor should have used, which would be just as subjective as having no "empirical" standard at all. We suggest removing the phrase "empirical information and" from the last sentence quoted.
43. Comparatively low rates of delinquency and default	Comment 43(c)(1)-1.ii.A.*2* provides that evidence that a creditor's ability-to-repay determination was reasonable and in good faith includes: "The creditor used underwriting standards that have historically resulted in comparatively low rates of delinquency and default	We request a definition of the term "comparatively low[.]" The comparison will vary greatly depending on which types of loans are compared, so additional guidance is needed on how to make the comparison. All delinquencies are defaults, but not all defaults are delinquencies.

252

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	during adverse economic conditions[.]"	Nonpayment defaults are irrelevant to ability to repay. The regulation should not apply to, or consider, defaults other than delinquencies. The same clarification is needed in comment 43(c)(1)-1.ii.B.*1*.
44. Reliance on consumer statements	Comment 43(c)(1)-1.i provides: "A consumer's statement or attestation that the consumer has the ability to repay the loan is not indicative of whether the creditor's determination was reasonable and in good faith."	We request clarification that a statement by a consumer that the information in a loan application or in another specified document is complete, accurate, and not misleading demonstrates the information about which the creditor was aware at closing, unless the consumer provides credible contrary evidence.
45. Evidence that an ability-to-repay determination was not reasonable or in good faith	Comment 43(c)(1)-1.ii.B.*1* provides that evidence that a creditor's ability-to-repay determination was not reasonable or in good faith may include: "The consumer defaulted on the loan a short time after consummation or, for an adjustable-rate, interest-only, or negative amortization mortgage, a short time after recast[.]"	A showing of inability to repay should require proof that, based on information on which the creditor reasonably relied, including information the consumer provided to the creditor, the creditor's determination was faulty. We recommend the following clarifications: • If a payment default was reasonably unforeseeable at or before consummation, that payment default should be *per se* irrelevant. • If a consumer directly or indirectly provided inaccurate information to a creditor who reasonably relied on it, the fact that it was inaccurate should be *per se* irrelevant to the question whether the creditor's ability-to-repay determination was proper.
46. Length of timely payments as an indicator of ability to repay	Comment 43(e)(1)(ii)-1 provides: "In addition, the longer the period of time that the consumer has demonstrated actual ability to repay the loan by making timely payments, without modification or accommodation, after consummation or, for an adjustable-rate mortgage, after recast, the less likely the consumer will be able to rebut the presumption based on insufficient residual income and prove that, at the time the loan was made, the creditor failed to make a reasonable and good faith determination that the consumer had the reasonable ability to repay	This will encourage consumers of QM loans outside the safe harbor to strategically make at least one late payment early after consummation to preserve the ability to rebut the presumption. This comment appears to assume that the payment increases after recast, and that the payments before recast are irrelevant. Some ARM loans with a long introductory period have an initial rate that is higher than the fully-indexed rate. We recommend clarification that rebutting the presumption requires

253

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	the loan."	showing *inability* to repay, and that mere nonpayment should be *per se* irrelevant. We recommend clarification that a strategic default is *per se* irrelevant. We recommend that timely payments on an ARM loan before recast should be evidence of ability to repay, even if the payment will increase after recast. That the payment will increase at recast is relevant, but so are a payment decrease after recast, and a pattern of making timely payments.
47. Verification of property taxes with government-provided information	Comment 43(c)(3)-5 provides: "With respect to the verification of mortgage-related obligations that are property taxes required to be considered under § 1026.43(c)(2)(v), a record is reasonably reliable if the information in the record was provided by a governmental organization, such as a taxing authority or local government. The creditor complies with § 1026.43(c)(2)(v) by relying on property taxes referenced in the title report if the source of the property tax information was a local taxing authority."	We request clarification that the phrase "provided by a governmental organization" means directly or indirectly provided by a governmental organization, such as in the title report example, but also in other cases, such as when a service provider obtains the information and provides it to a creditor.
48. Debt or liability specified in appendix Q	Comment 43(e)(2)(v)-3 provides: "Section 1026.43(e)(2)(v)(B) requires creditors to consider and verify the consumer's current debt obligations, alimony, and child support. For purposes of this requirement, the creditor must consider and verify, at a minimum, any debt or liability specified in appendix Q. A creditor may also consider and verify other debt in accordance with § 1026.43(c)(2)(vi) and (c)(3); however, such debt would not be included in the total monthly debt-to-income ratio determination required by § 1026.43(e)(2)(vi)."	We request clarification of the term "any debt or liability specified in appendix Q." Appendix Q uses the terms liabilities, recurring obligations, other continuing obligations, and contingent liabilities. Is each of these a "current debt obligation" within the meaning of § 43(e)(2)(v)-3? Or are these appendix Q terms limited to current debt obligations?

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
49. DTI calculation in § 43(e)(2)(vi) and appendix Q	Under § 43(e)(2)(vi), QM loans must have a DTI not exceeding 43 percent. Section 43(e)(2)(vi) provides: "For purposes of this paragraph (e)(2)(vi), the ratio of the consumer's total monthly debt to total monthly income is determined: (A) Except as provided in paragraph (e)(2)(vi)(B) of this section, in accordance with the standards in appendix Q; (B) Using the consumer's monthly payment on: *(1)* The covered transaction, including the monthly payment for mortgage-related obligations, in accordance with paragraph (e)(2)(iv) of this section; and *(2)* Any simultaneous loan that the creditor knows or has reason to know will be made, in accordance with paragraphs (c)(2)(iv) and (c)(6) of this section." Comment 43(e)(2)(vi) provides: "As provided in appendix Q, for purposes of § 1026.43(e)(2)(vi), creditors must include in the definition of 'debt' a consumer's monthly housing expense. This includes, for example, the consumer's monthly payment on the covered transaction (including mortgage-related obligations) and on simultaneous loans. Accordingly, § 1026.43(e)(2)(vi)(B) provides the method by which a creditor calculates the consumer's monthly payment on the covered transaction and on any simultaneous loan that the creditor knows or has reason to know will be made."	We request clarification of the specific provisions within appendix Q to which § 43(e)(2)(vi)(A) refers. We request clarification that the comment language means: "~~As provided in appendix Q, f~~For purposes of § 1026.43(e)(2)(vi), creditors must include in the definition of 'debt' a consumer's monthly housing expense. This **housing expense** includes~~, for example,~~ **only** the consumer's monthly payment on the covered transaction (including mortgage-related obligations) and on simultaneous loans."
50. Contingent liabilities	Comment 43(c)(2)(vi)-2 provides:	We request clarification of whether the potential liability of an applicant for a non-QM loan as a surety or guarantor under a different

255

TOPIC	PROVISION	RECOMMENDATION
	"If one consumer [of multiple applicants] is merely a surety or guarantor, § 1026.43(c)(2)(vi) does not require a creditor to consider the debt obligations of such surety or guarantor." Comment 43(c)(2)(viii)-2 provides: "When two or more consumers apply for an extension of credit as joint obligors with primary liability on an obligation, § 1026.43(c)(2)(viii) requires a creditor to consider the credit history of all such joint applicants. If a consumer is merely a surety or guarantor, § 1026.43(c)(2)(viii) does not require a creditor to consider the credit history of such surety or guarantor."	loan should be included in the applicant's debt obligations.
51. Verification of simultaneous loan by promissory note	Comment 43(c)(3)-4 provides: "If the creditor knows or has reason to know that there will be a simultaneous loan extended at or before consummation, the creditor may verify the simultaneous loan by obtaining third-party verification from the third-party creditor of the simultaneous loan. For example, the creditor may obtain a copy of the promissory note or other written verification from the third-party creditor. For further guidance, see comments 43(c)(3)–1 and –2 discussing verification using third-party records." The referenced comments do not relate to simultaneous loans. The relevant portions provide: "Records a creditor uses for verification under § 1026.43(c)(3) and (4) must be specific to the individual consumer. . . . A creditor also may obtain third-party records directly from the consumer, likewise	The suggestion that a creditor verify a loan that has not closed by obtaining the promissory note is unclear because the note will not exist. The creditor of an intended simultaneous loan may not provide verification for any reason, including that the existence and terms of the loan are not yet certain. We request clarification that when a third-party creditor of a simultaneous loan does not provide verification, the creditor may rely instead on a borrower's statement about the fact of, and the terms of, any simultaneous loan. If available from the consumer, the creditor should be able to rely on a copy of the application for the simultaneous loan.

TOPIC	PROVISION	RECOMMENDATION
	as long as the records are reasonably reliable and specific to the individual consumer."	
52. Water bills should be excluded from mortgage-related obligations	Comment 43(b)(8)-2 includes property taxes, defined broadly, in mortgage-related obligations: "Section 1026.43(b)(8) includes obligations that are equivalent to property taxes, even if such obligations are not denominated as 'taxes.' For example, governments may establish or allow independent districts with the authority to impose levies on properties within the district to fund a special purpose, such as a local development bond district, water district, or other public purpose. These levies may be referred to as taxes, assessments, surcharges, or by some other name. For purposes of § 1026.43(b)(8), these are property taxes and are included in the determination of mortgage-related obligations."	Certain services, such as water, sewer or trash services may be provided by either a private company or a government. Where a government imposes charges for such services, the charges should be explicitly excluded from mortgage-related obligations because they have no relation to the mortgage loan.
53. Roommate or boarder	As it would be amended by the CFPB's April 19, 2013 proposed rulmaking, appendix Q § II.D.3 would read: "a. Income from roommates in a single family property occupied as the consumer's primary residence is not acceptable. Rental income from boarders however, is acceptable. b. The rental income may be considered effective, if shown on the consumer's tax return. If not on the tax return, rental income paid by the boarder may not be used in qualifying."	We recommend defining the terms roommate and boarder so that the differences between the terms are known.
	Refinance of Nonstandard Loan	
54. Use of proceeds of standard mortgage	Section 43(d)(1)(ii)(E) provides that proceeds of a standard mortgage may be used only to pay off the nonstandard loan and to pay closing costs required to be disclosed under RESPA. Comment 43(d)(1)(ii)(E)-1 provides:	We suggest the proceeds also be able to be used to pay for a payoff statement and a lien release on the nonstandard loan, and, for a shared appreciation nonstandard loan, an appraisal to determine the payoff amount. These would be consistent with the intent of the regulation and

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	"If the proceeds of a covered transaction are used for other purposes, such as to pay off other liens or to provide additional cash to the consumer for discretionary spending, the transaction does not meet the definition of a 'standard mortgage.'"	comment.
55. Thirty days as "generally" a reasonable amount of time	Under § 43(d)(5)(i)(A), in calculating the payment on a nonstandard mortgage, creditors may use the fully-indexed rate as of a reasonable of time before or after the creditor receives the application. Comment 43(d)(5)(i)-2 provides: "Thirty days is **generally** considered 'a reasonable period of time'" (emphasis added).	We recommend removing the word "generally" because it creates substantial uncertainty for no apparent reason. If the word remains, we request clarification of all circumstances under which thirty days would not be a reasonable amount of time. When thirty days is not a reasonable amount of time, we request clarification of how the creditor is to know what is reasonable. Refinancing nonstandard loans that the borrowers can afford into standard loans with materially lower payments are a clear borrower benefit and do not raise ability-to-repay concerns. There should be as few restrictions on this consumer benefit as is reasonably possible.
56. Payment calculation for nonstandard loan – relevance of actual prepayments	In calculating the payment on a nonstandard loan under § 43(d)(5)(i), it is not clear whether the creditor must take into account any actual prepayments on the nonstandard loan. For IO loans, § 43(d)(5)(i)(C)(*2*) directs the creditor to base the calculation of the payment on a nonstandard loan on: "[T]he outstanding principal balance as of the date of the recast, assuming all scheduled payments have been made up to the recast date and the payment due on the recast date is made and credited as of that date[.]" Comment 43(d)(5)(i)-6 provides:	We request clarification of the calculation for a nonstandard loan on which the consumer has made optional prepayments before recast.

258

TOPIC	PROVISION	RECOMMENDATION
	"First, the payment must be based on the outstanding principal balance as of the date of the recast, assuming all scheduled payments are made under the terms of the legal obligation in effect before the mortgage is recast. For a loan on which only interest and no principal has been paid, the outstanding principal balance at the time of recast will be the loan amount, as defined in § 1026.43(b)(5), assuming all scheduled payments are made under the terms of the legal obligation in effect before the mortgage is recast. For example, assume that a mortgage has a 30-year loan term, and provides that the first 24 months of payments are interest-only. If the 24th payment is due on September 1, 2015, the creditor must calculate the outstanding principal balance as of September 1, 2015, assuming that all 24 payments under the interest-only payment terms have been made and credited timely and that no payments of principal have been made." Even if all scheduled payments are made, it is possible that the borrower made some optional prepayments. The example in this comment assumes the consumer has made no principal payments, and the example in comment 43(d)(5)(i)-7 also assumes the consumer has made no principal payments. The explanation of the issue concerns an IO loan, but the same question arises for actual prepayments on a nonstandard ARM loan. For negative amortization loan, comment 43(d)(5)(i)-8.i provides: "If the consumer makes payments above the minimum periodic payments for the maximum possible time, the creditor must calculate the maximum loan amount based on the outstanding principal	

259

TOPIC	PROVISION	RECOMMENDATION
	balance." It is unclear why this example is limited to a consumer who makes payments above the minimum requirement "for the maximum possible time" as opposed to a shorter period. Is this the only circumstance in which the creditor must consider the actual outstanding principal balance?	
Loan Originator Compensation and Qualification		
57. Revising compensation plans	Comment 36(d)(1)-6 (in the loan originator compensation rule) provides: "Section 1026.36 does not limit a creditor or other person from periodically revising the compensation it agrees to pay a loan originator. However, the revised compensation arrangement must result in payments to the loan originator that are not based on the terms of a credit transaction. A creditor or other person might periodically review factors such as loan performance, transaction volume, as well as current market conditions for originator compensation, and prospectively revise the compensation it agrees to pay to a loan originator."	How often can compensation change, and can it change in response to loan production?
58. Long term loan performance	Comment 36(d)(1)-2.i.B permits compensation based on the long-term performance of an originator's loans.	What is the definition of long-term performance? If a loan originator will receive a payment each month after origination that the loan is not delinquent, would all such payments be considered payments for long-term loan performance?
Appendix Q		
59. Applicability	Appendix Q is entitled *Appendix Q to Part 1026—Standards for Determining Monthly Debt and Income.*	We request confirmation that appendix Q applies only to § 43(e)(2)(v) and (vi), and that it does not apply to debt and income determinations under § 43(c).

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
60. Verification of part-time employment	Appendix Q § I.A.3.a.iv provides that creditors must examine the "employer's confirmation of continued employment." Section I.B.4.a provides: "Part-time and seasonal income can be used to qualify the consumer if the creditor documents that the consumer has worked the part-time job uninterrupted for the past two years, and plans to continue. Many low and moderate income families rely on part-time and seasonal income for day to day needs, and creditors should not restrict consideration of such income when qualifying these consumers."	We request clarification that if an application lists part-time employment and if the verification of employment has no evidence that employment is not going to continue, that the creditor has adequately documented that the income will continue.
61. Conclusive evidence of no debt collection	Appendix Q § IV.2 provides: "The contingent liability policies described in this topic apply unless the consumer can provide conclusive evidence from the debt holder that there is no possibility that the debt holder will pursue debt collection against him/her should the other party default."	We request confirmation that copies of cancelled checks that the debt holder cashed are sufficient, even if they are not obtained from the debt holder.
62. Income reasonably expected to continue	The CFPB proposes to remove language from § I.B.1.a about income reasonably expected to continue "through at least the first three years of the mortgage loan."	We request clarification of how far into the future creditors must reasonably expect income to continue.
63. Cost of tax transcripts	The CFPB has proposed to remove two statements, in §§ I.B.7 note iii and I.C, that the cost of the transcript may be charged to the consumer.	We request clarification that that this change does not prohibit the creditor from charging the consumer for the transcript if otherwise permitted by law.
	Other	
64. Definition of "offer" for alternative offer	Section 43(g)(3) provides: "A creditor must not offer a consumer a covered transaction with a prepayment penalty unless the creditor also offers the consumer an alternative covered transaction without a prepayment penalty . . . ."	When a loan is offered is not clear. We suggest clarification that a creditor may comply by documenting that the creditor made the consumer aware of the alternative covered transaction.
65. Fully-indexed rate for	Comment 43(c)(5)(i)-5.iii describes a "fully-indexed rate" for a step-rate	We recommend clarification that step-rate loans do not have a fully-

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
step-rate loans	loan: "A loan in an amount of $200,000 has a 30-year loan term. The loan agreement provides that the interest rate will be 6.5 percent for the first two years of the loan, 7 percent for the next three years of the loan, and 7.5 percent thereafter. Accordingly, the scheduled payment amounts are $1,264 for the first two years, $1,328 for the next three years, and $1,388 thereafter for the remainder of the term. For purposes of § 1026.43(c)(2)(iii), the creditor must determine the consumer's ability to repay the loan based on a payment of $1,398, which is the substantially equal, monthly, fully amortizing payment that would repay $200,000 over 30 years using the fully indexed rate of 7.5 percent." Section 43(b)(3) defines a fully-indexed rate as a rate that applies after recast, and recast is not defined for step-rate loans.	indexed rate, and that their payment calculation under § 43(c)(5)(i) uses the maximum rate that may apply during the loan term. Otherwise, § 43(c)(5)(i)(A) would appear to use the introductory rate on a step-rate loan, which was not the intent.
66. Nonjudicial foreclosure	Section 36(h) provides: "A contract or other agreement for a consumer credit transaction secured by a dwelling (including a home equity line of credit secured by the consumer's principal dwelling) may not include terms that require arbitration or any other non-judicial procedure to resolve any controversy or settle any claims arising out of the transaction."	We request confirmation that this does not prohibit nonjudicial foreclosure in the event of any default.
67. FHA or Regulation Z definition of loan amount	Section 32(b)(1)(i)(C)(2) includes upfront PMI premiums in points and fees only if the premiums exceed an FHA premium amount: "If the premium or other charge is payable at or before consummation, [points and fees exclude] the portion of any such	When calculating what portion of a non-FHA upfront MIP is included in points and fees in Regulation Z, we request clarification and examples of how to calculate the loan amount, and whether it varies based on whether the borrower finances the upfront MIP.

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	premium or other charge that is not in excess of the amount payable under policies in effect at the time of origination under section 203(c)(2)(A) of the National Housing Act (12 U.S.C. 1709(c)(2)(A)), provided that the premium or charge is required to be refundable on a pro rata basis and the refund is automatically issued upon notification of the satisfaction of the underlying mortgage loan[.]" FHA upfront premiums are calculated as a percentage of the "base loan amount" without the premium even if the borrower finances it. FHA Mortgagee Letter 2012-4 provides: "FHA will continue to permit financing of this [upfront MIP] charge into the mortgage and will continue to calculate actual premium charges against the base loan amount before adding any financed UFMIP." Section 32(b)(4)(i) defines the total loan amount as: "The total loan amount for a closed-end credit transaction is calculated by taking the amount financed, as determined according to § 1026.18(b), and deducting any cost listed in § 1026.32(b)(1)(iii) [4(c)(7) fees], (iv) [credit insurance, etc] or (vi) [prepayment penalties] that is both included as points and fees under § 1026.32(b)(1) and financed by the creditor." The referenced § 18(b) defines "amount financed" to include the principal loan amount:	The borrower may not decide whether to finance an MIP or pay it at closing until late in the origination process. Creditors need to know the amount of points and fees as early as possible. For this reason, we recommend that the amount included in points and fees may be calculated as if the consumer will finance the amount, even if the consumer later decides not to do so. [We have reached out to the mortgage insurance industry for a recommendation on how to resolve this question. We will update this document when we receive feedback.]

LOWER PRIORITY

TOPIC	PROVISION	RECOMMENDATION
	"The amount financed is calculated by: (1) Determining the principal loan amount or the cash price (subtracting any downpayment); (2) Adding any other amounts that are financed by the creditor and are not part of the finance charge; and (3) Subtracting any prepaid finance charge." This definition deducts amounts financed only if they are not part of the finance charge. MIPs are part of the finance charge, § 4(b)(5), meaning that, under § 32(b)(4)(i), MIPs are included in the amount financed if the borrower finances them. Section 43(b)(5) defines loan amount as: "*Loan amount* means the principal amount the consumer will borrow as reflected in the promissory note or loan contract." If a borrower finances a finance charge item, such as an upfront MIP, it may or may not be included in the promissory note. *See* comment 18(b)(3).	
68. Typographical error	Comment 43(c)(5)(i)-5.iii gives an example of the same payment amount on a loan, once as $1388 and once as $1398. Both should be $1398.	

ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

June 18, 2013

Qualified Mortgage Rule Will Jeopardize Access to Credit

On behalf of the 7,000 community banks represented by the Independent Community Bankers of America (ICBA), thank you for convening today's hearing titled: "Examining How the Dodd-Frank Act Hampers Home Ownership." We appreciate the opportunity to submit this statement for the record.

Reform of the Consumer Financial Protection Bureau's qualified mortgage/ability-to-repay ("QM") rule is a key plank of ICBA's Plan for Prosperity: A Regulatory Relief Agenda to Empower Local Communities. ICBA Chairman William A. Loving, Jr. detailed our concerns with the QM rule in his testimony at your April 16 hearing on community bank regulatory burden. Since that hearing, on May 29, the CFPB issued amendments to QM rule which make accommodations for community banks. While ICBA supports these amendments, they do not go far enough to preserve access to credit for community bank customers. The Plan for Prosperity calls for legislation that would provide safe harbor QM status for community bank loans held in portfolio, including balloon loans in rural and non-rural areas and without regard to their pricing. This legislative proposal is discussed in more detail later in this statement.

Balloon Mortgages Play Essential Role in Rural Communities

Community banks are responsible mortgage lenders that did not participate in the abuses that contributed to the financial crisis. Community banks help borrowers in rural communities where non-traditional loans such as balloon mortgages are prevalent due to the unique nature of rural properties. These loans are not eligible to be sold into the secondary market and are kept in portfolio, which gives community banks a vested interest in the quality of these loans and allows them to work out a solution directly with the borrower if repayment problems arise.

QM Rule Does Not Adequately Protect Community Bank Balloon Mortgages

While the CFPB's QM rule allows balloon loans made by small creditors that operate predominantly in rural or underserved areas to be qualified mortgages, the Bureau's definition of "rural" is too narrow and assumes an entire county is either rural or non-rural, which is inherently inaccurate. As a result, too many communities are denied rural status and unnecessarily cut off from access to credit. When a balloon loan does not receive QM safe harbor protection, the lender is exposed to undue litigation risk. Many community banks are not willing to assume that risk and will exit the mortgage lending business. The CFPB's recent amendment to the QM rule provides a two-year transition period during which balloon loans made by "non-rural" lenders can obtain QM status.

Attached to this statement is a state-by-state map of rural county designations. Members of this committee may be surprised at the rural county designations within their own states and concerned that many areas of the state are not covered. Also attached is ICBA's recent Community Bank Qualified Mortgage Survey, which underscores the significance of balloon loans to community bank customers and the failure of the CFPB's definition of "rural" to protect these loans.

A Clean Fix is Needed

As an alternative to the CFPB's QM rule, ICBA is pressing for a clean solution that avoids complex and unbalanced rural designations. Our preferred solution relies on the natural incentive of lenders to ensure that loans held in portfolio are affordable to the borrower and to work with the borrower should they encounter difficulty in repayment.

ICBA's Plan for Prosperity solution to this new regulatory threat is simple, straightforward, and will preserve the community bank lending model: Safe harbor QM status for community bank loans held in portfolio, including balloon loans in rural and non-rural areas and without regard to their pricing. When a community bank holds a loan in portfolio it holds 100 percent of the credit risk and has every incentive to ensure it understands the borrower's financial condition and to work with the borrower to structure the loan properly and make sure it is affordable. Withholding safe harbor status for loans held in portfolio, and exposing the lender to litigation risk, will not make the loans safer, nor will it make underwriting more conservative, it will merely deter community banks from making such loans in the many counties that do not meet the definition of rural.

The CLEAR Relief Act

ICBA thanks Representative Blaine Luetkemeyer, a former community banker, for including a provision in the CLEAR Relief Act (H.R. 1750) that would accord QM status to mortgages originated and held in portfolio for at least three years by a lender with less than $10 billion in assets. ICBA strongly supports the CLEAR Relief Act because it contains this provision in addition to other key mortgage and non-mortgage provisions of the Plan for Prosperity, and we encourage this committee to consider it.

Thank you again for the opportunity to submit this statement for the record. ICBA looks forward to working with this committee to reform the QM rule to properly recognize the importance to our rural economies and housing market of balloon loans originated by community banks and held in portfolio.

Attachments

- **State-By-State Rural County Designation Maps** (blue counties are rural; yellow are non-rural)
- **Community Bank Qualified Mortgage Survey**

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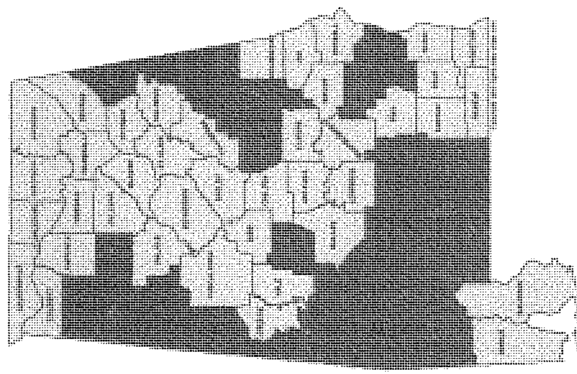
State-by-State Impact of CFPB "Rural" Definition

Rural (blue) and Non-Rural (yellow) Counties Under the Consumer Financial Protection Bureau's Final "Ability to Repay" Rule



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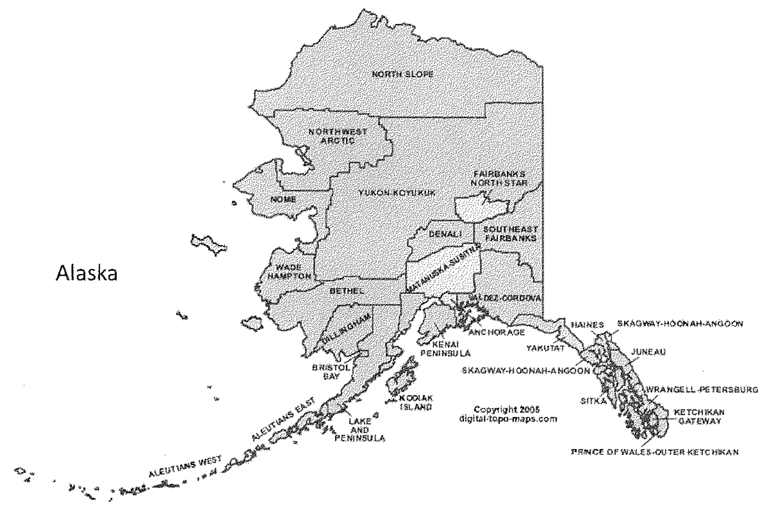
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KETCHIKAN GATEWAY
PRINCE OF WALES-OUTER KETCHIKAN
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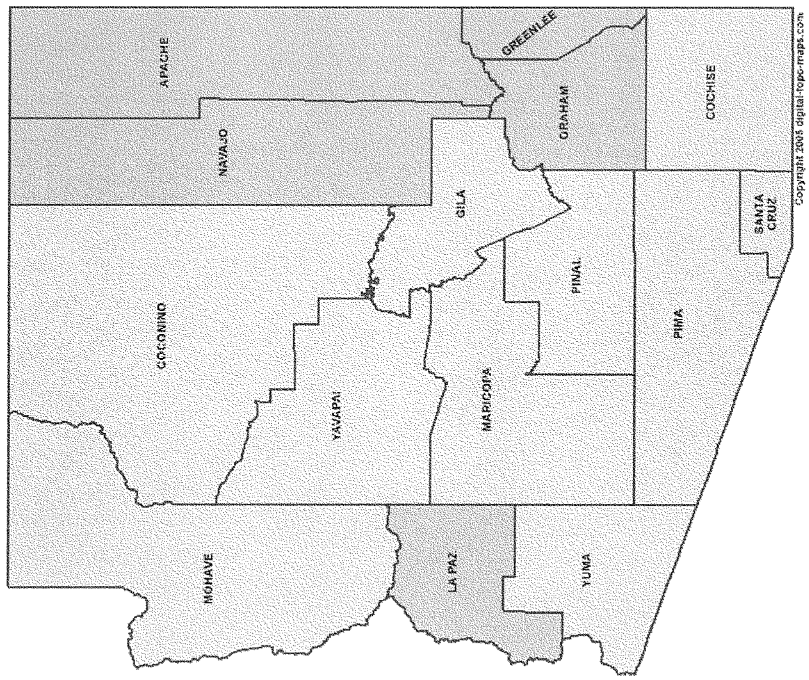
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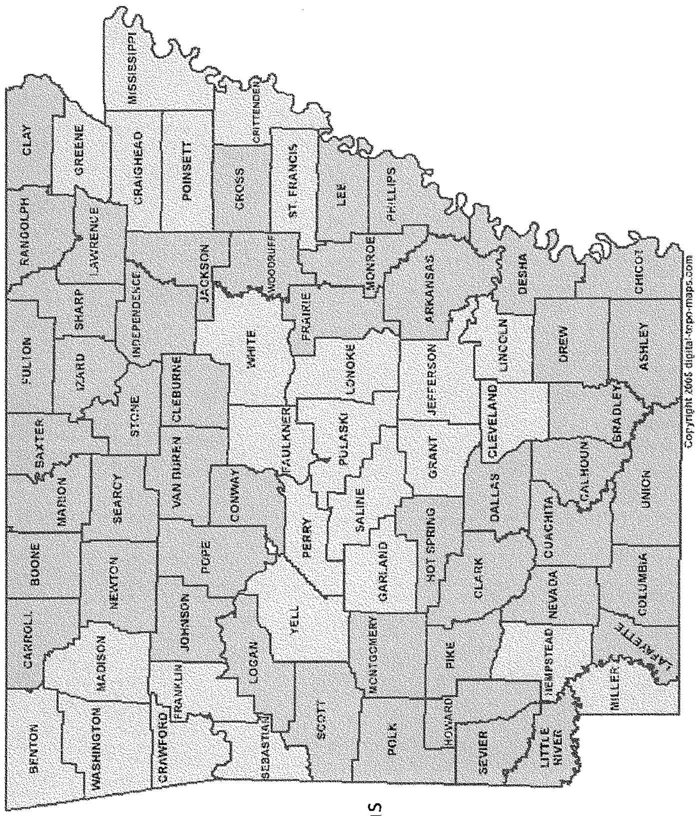
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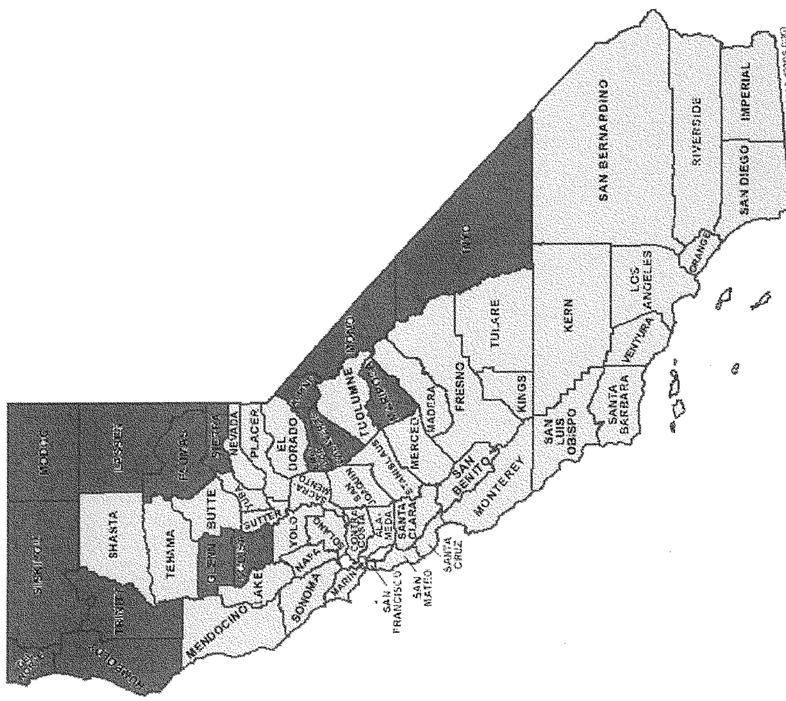
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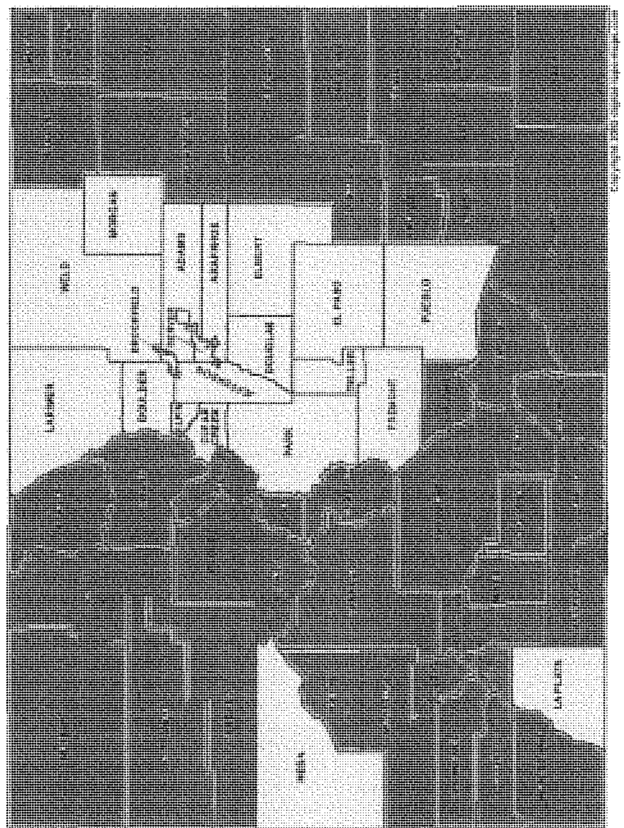

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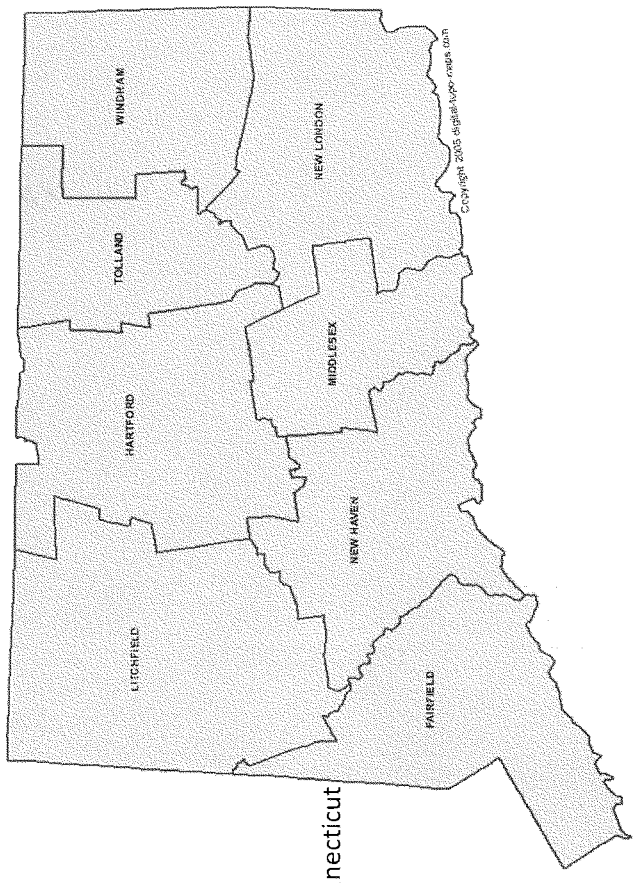

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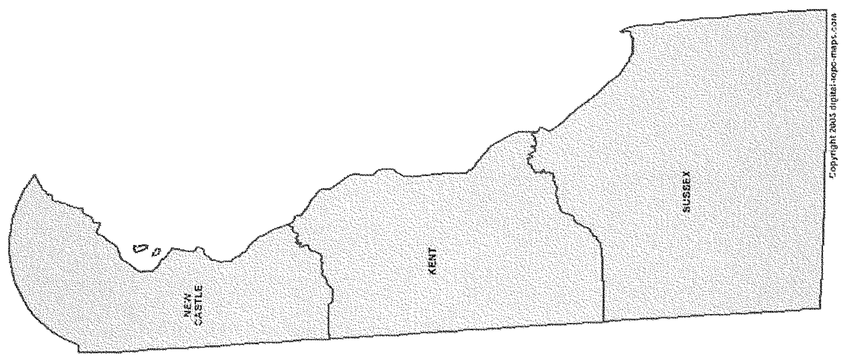
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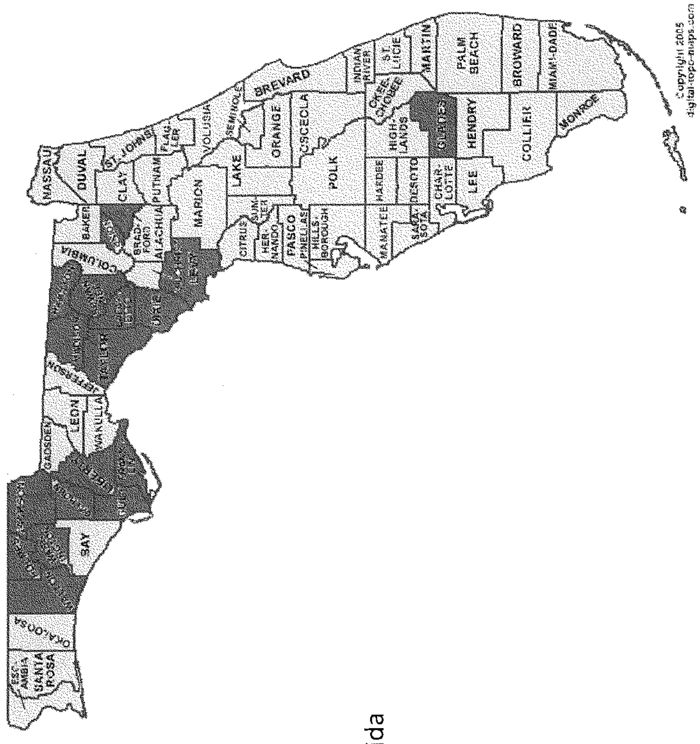
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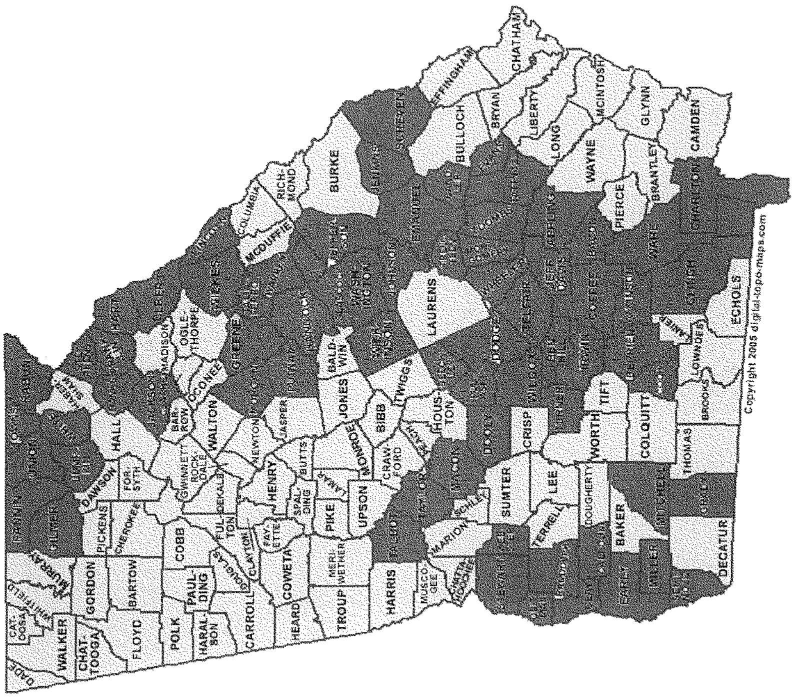
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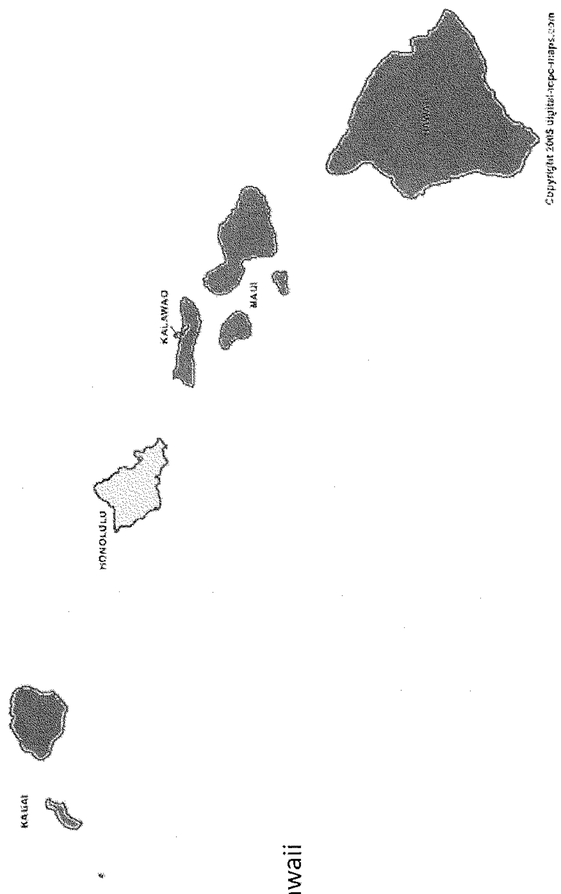

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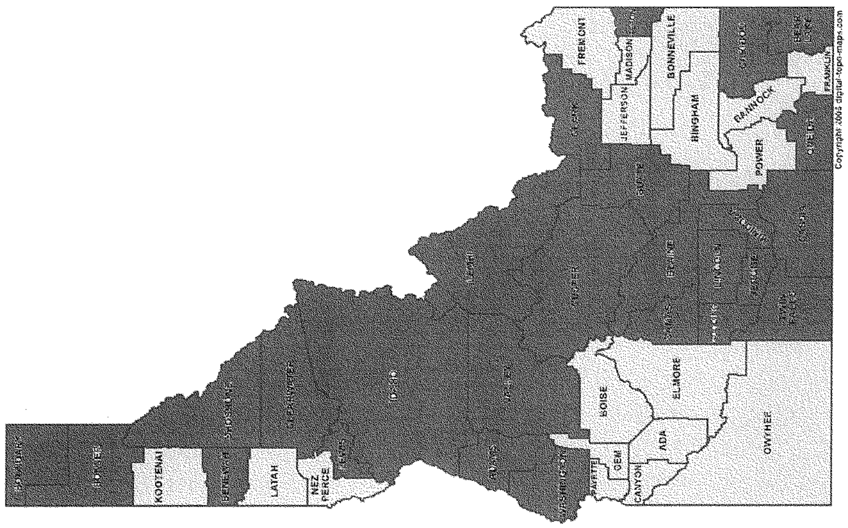
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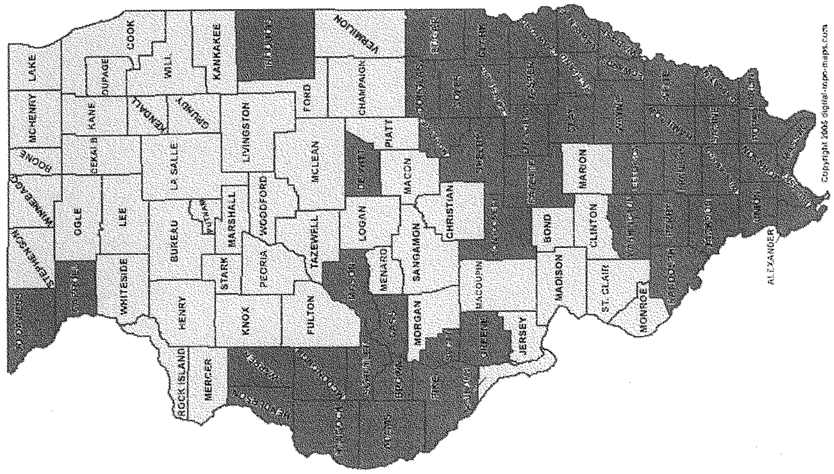
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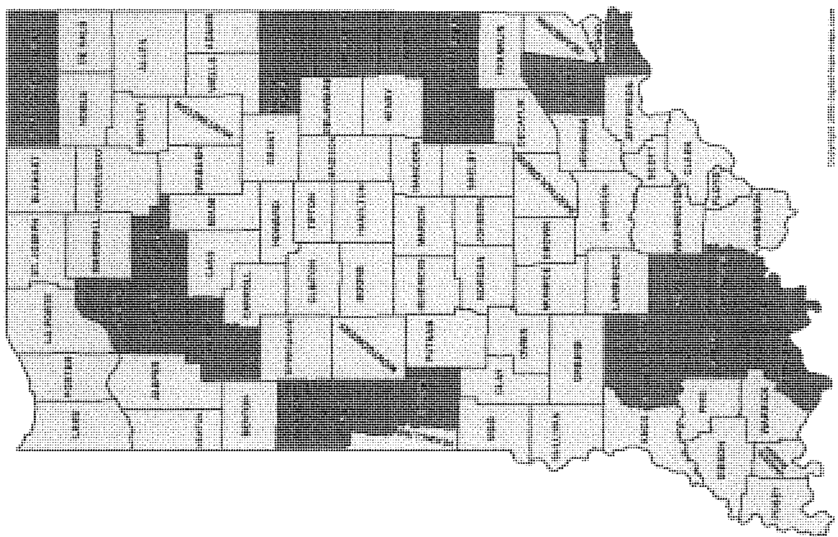

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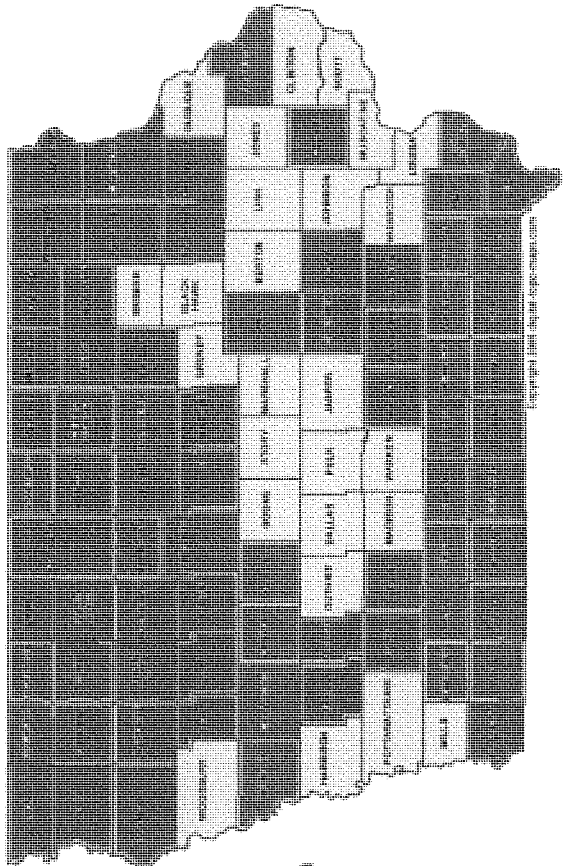

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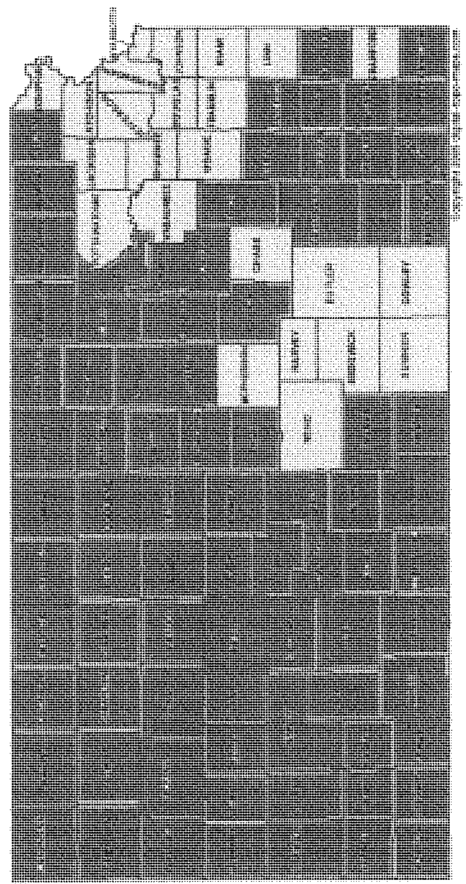

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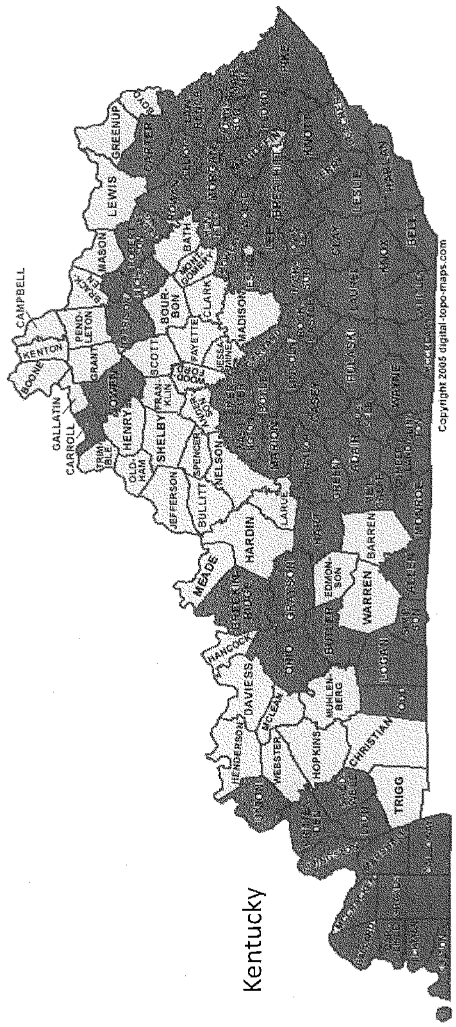
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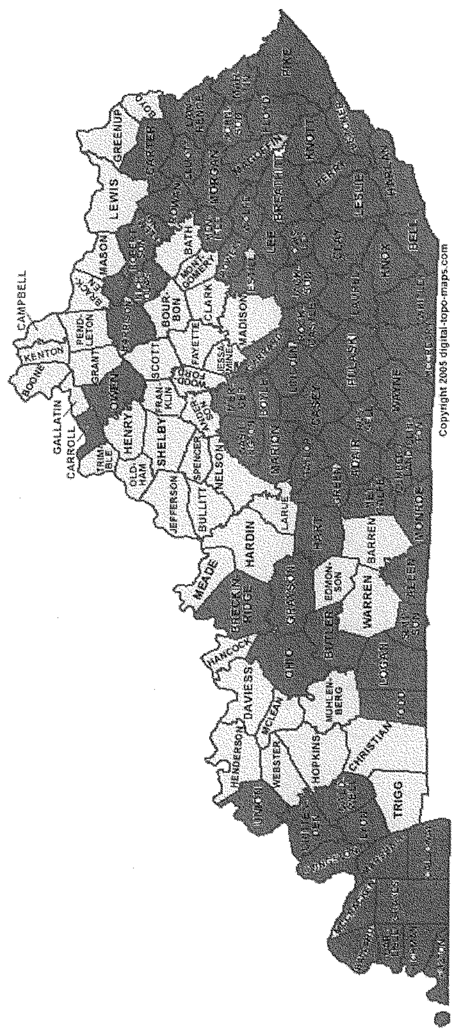
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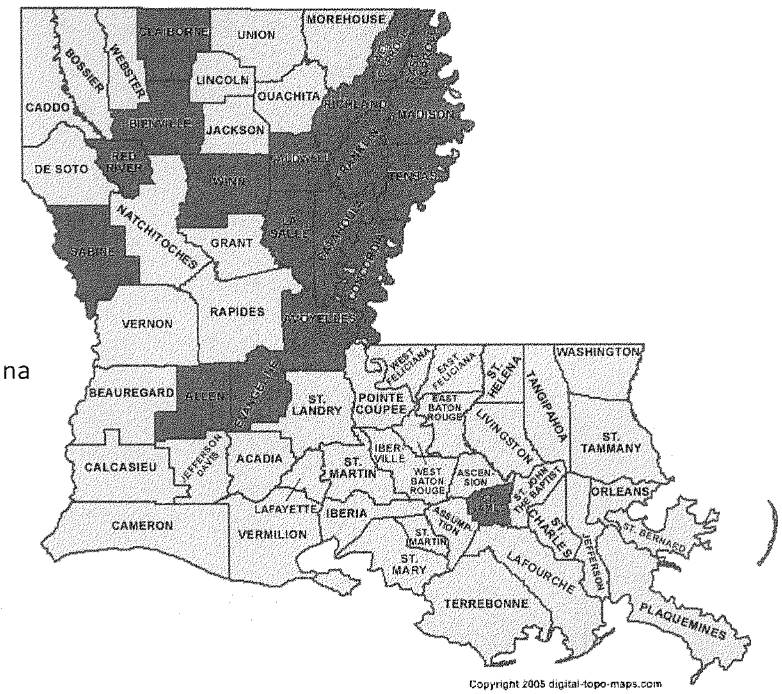
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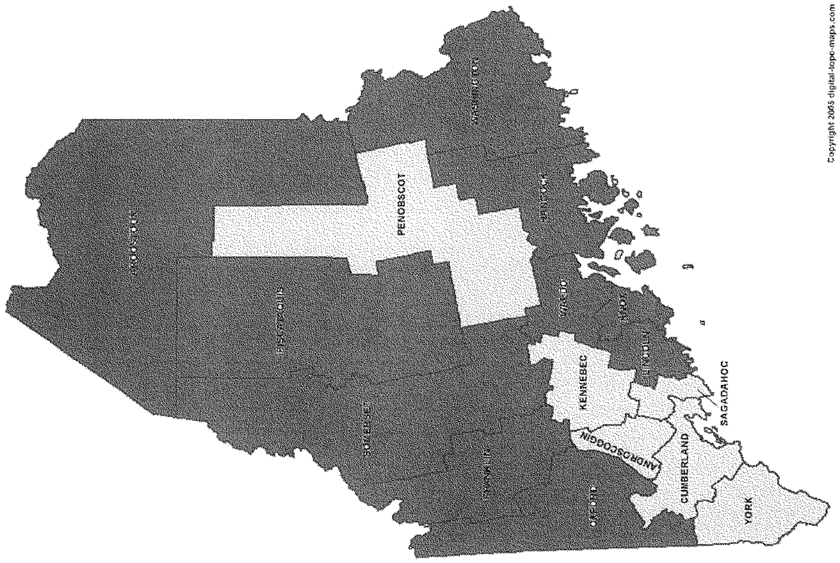
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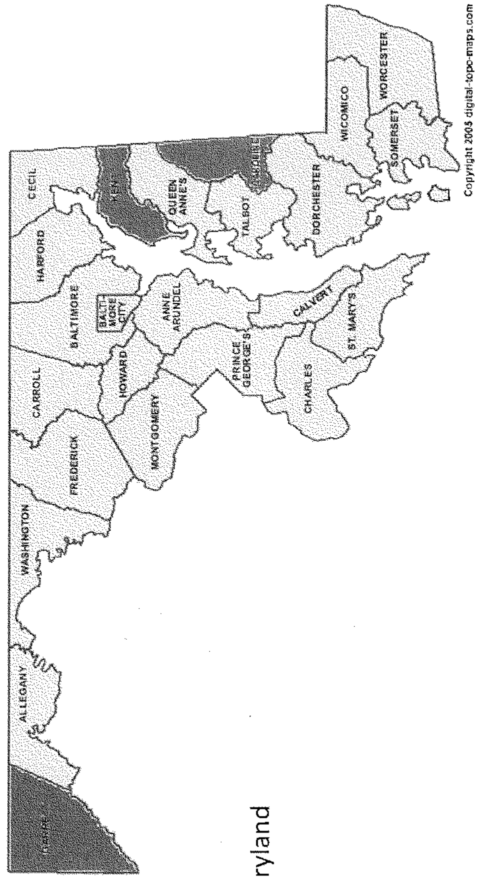
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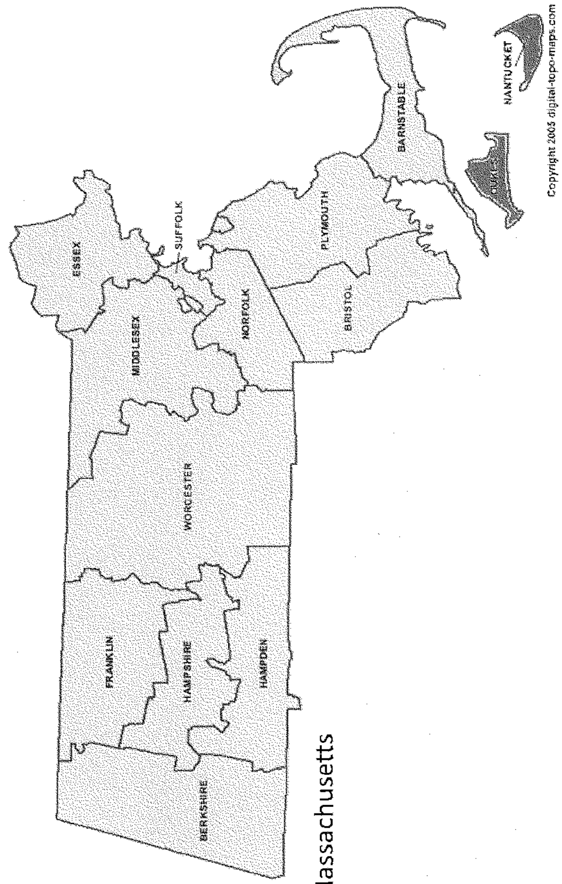

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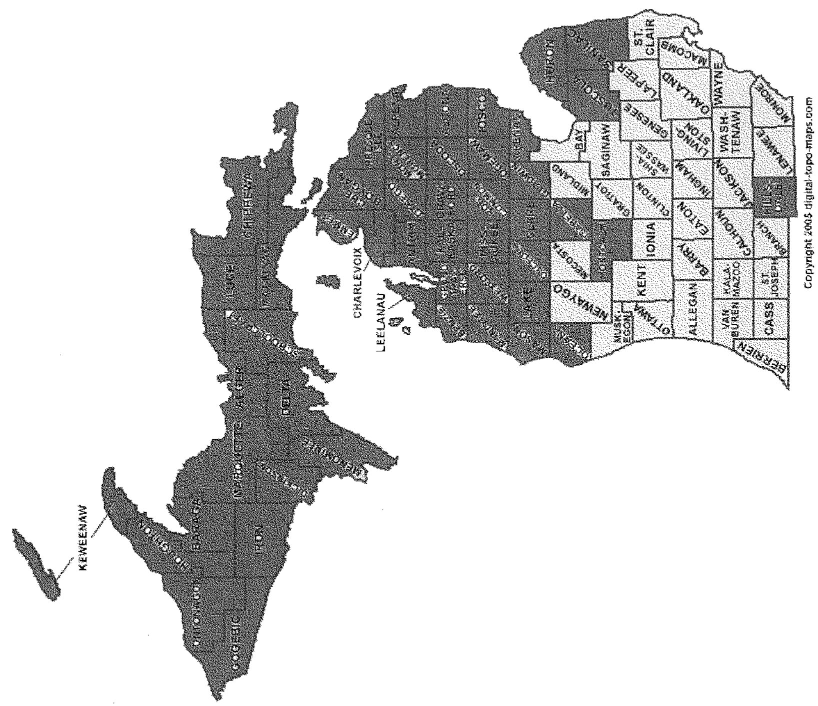
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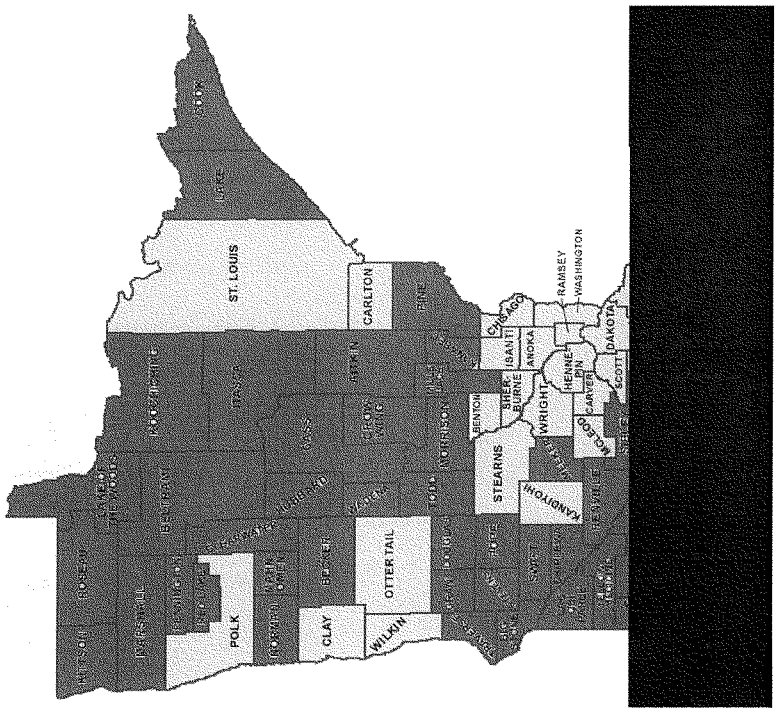
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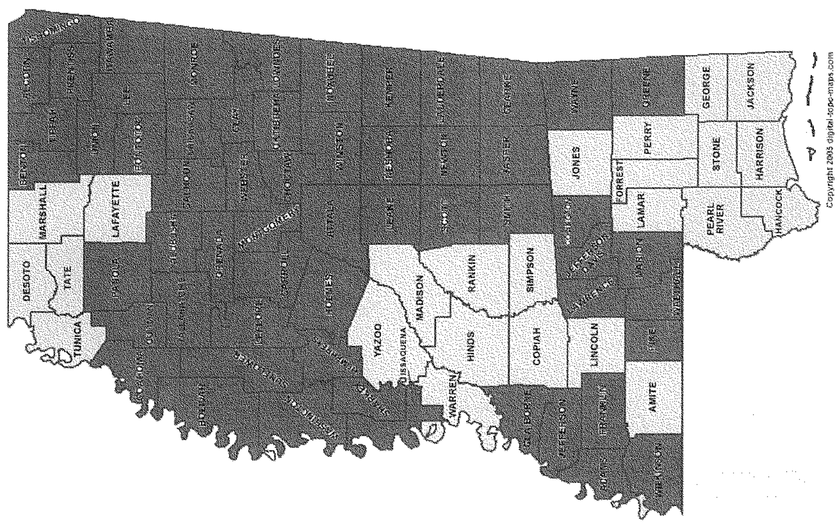

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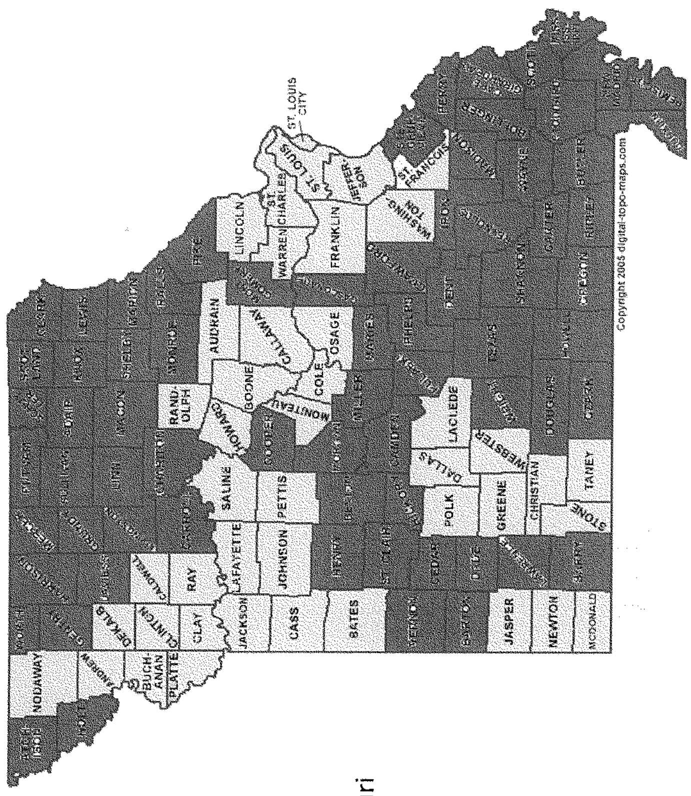
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BOONE
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HOWARD
MONITEAU
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POLK
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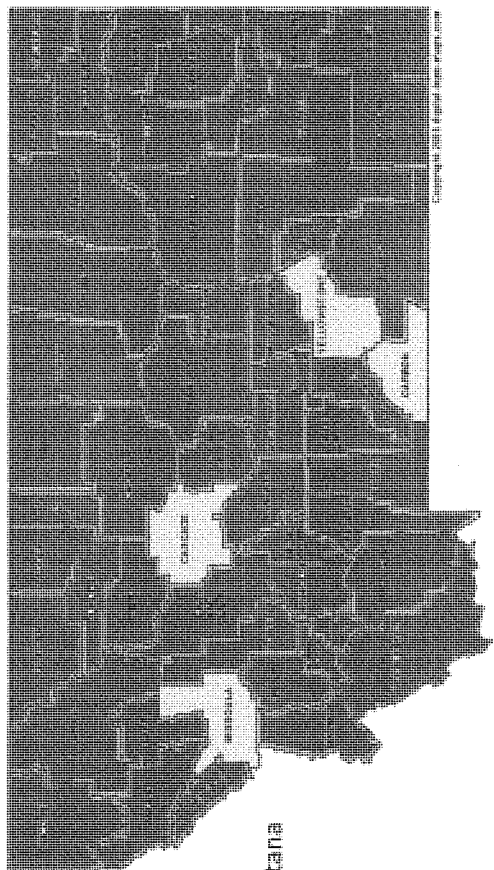

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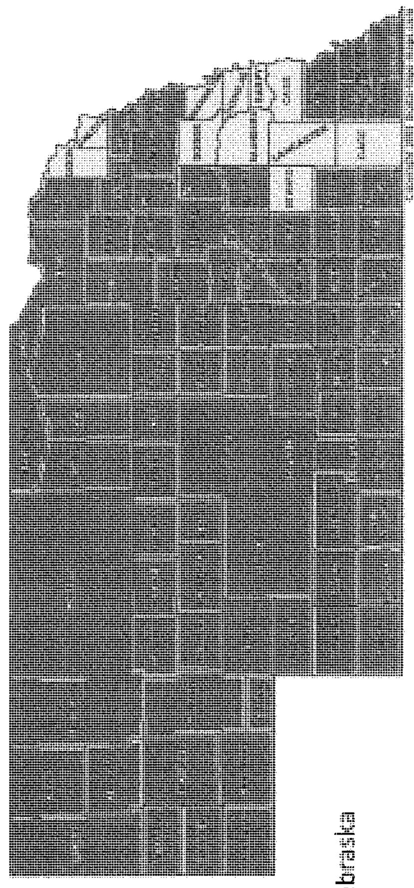

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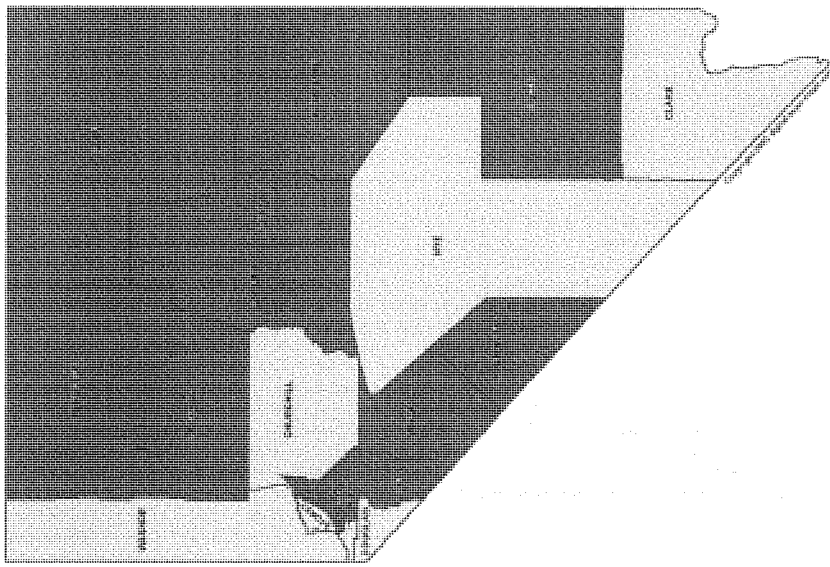

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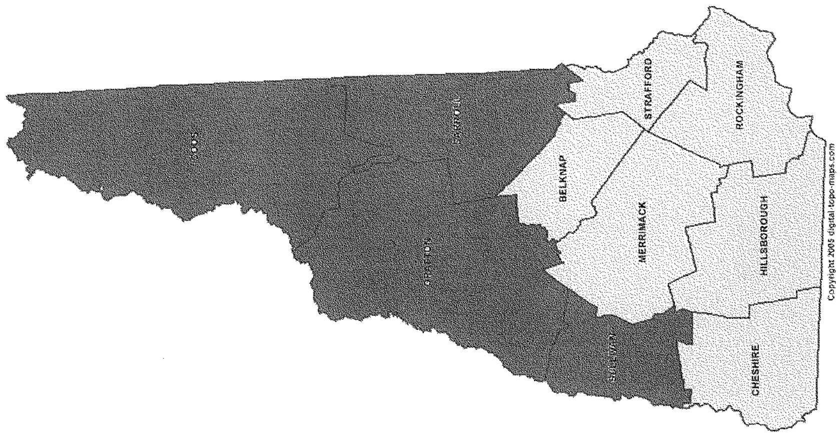

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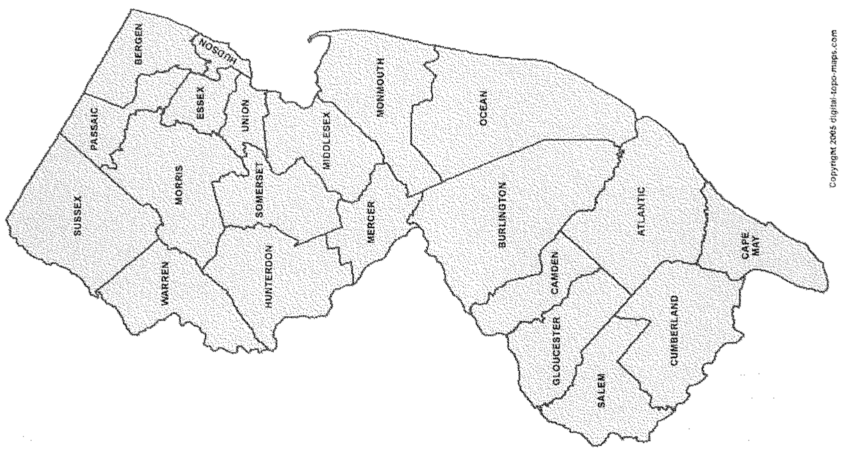
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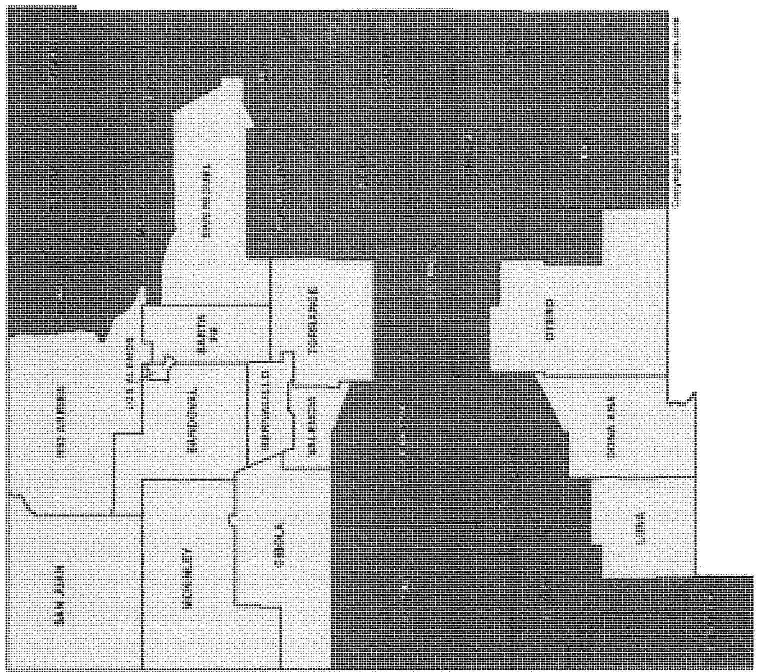

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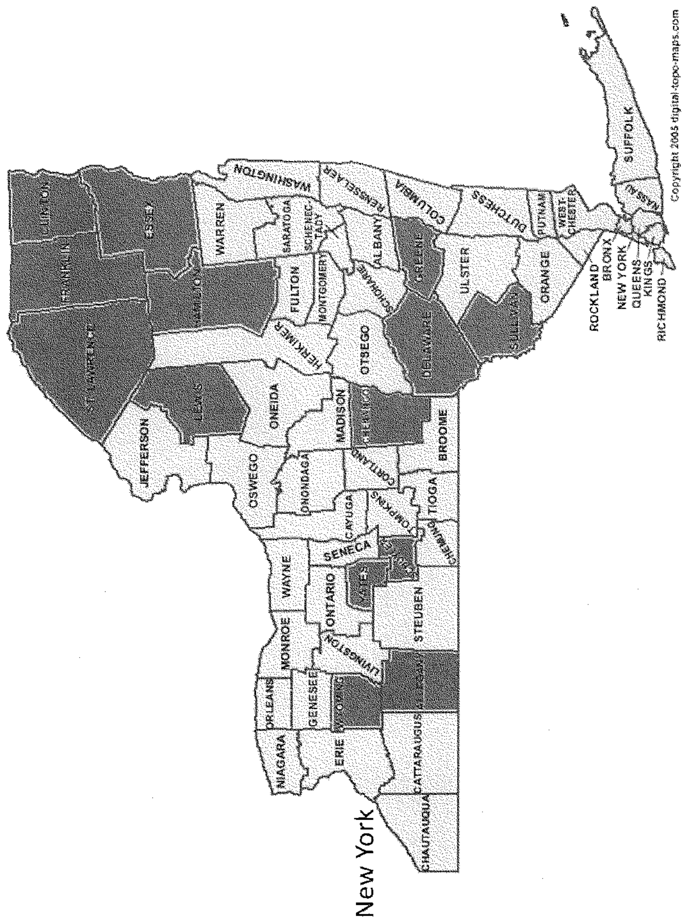
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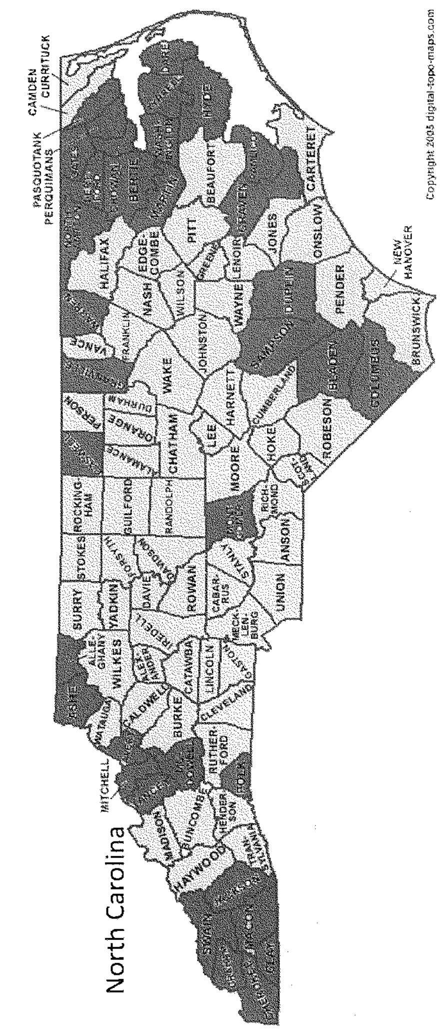
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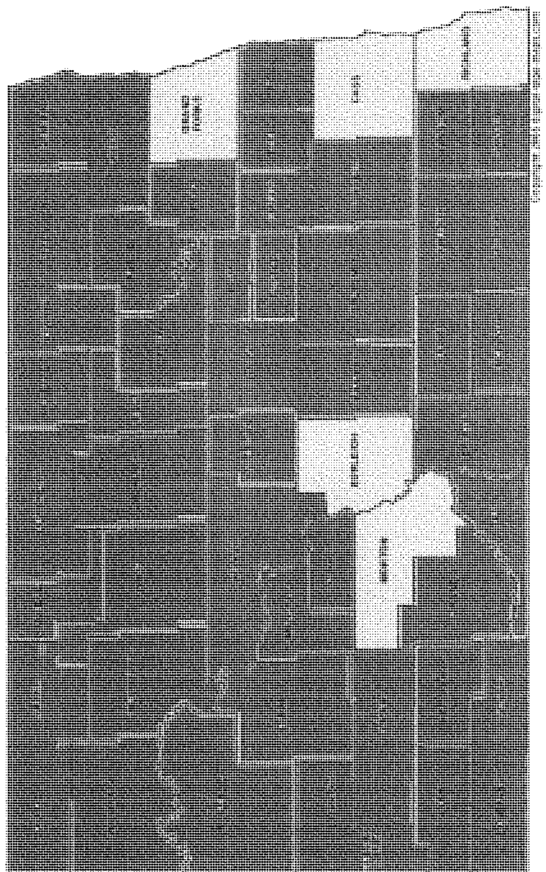

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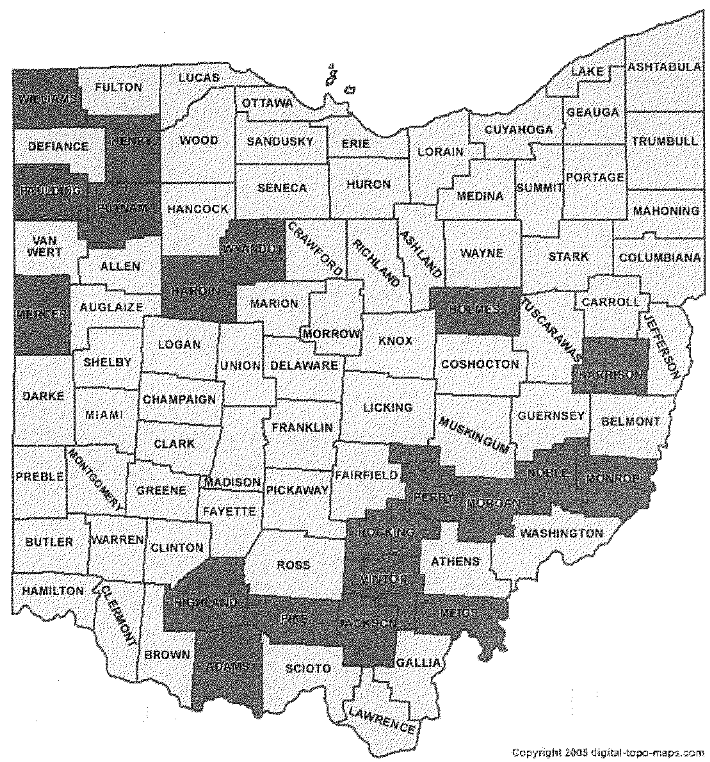
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STARK
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HARDIN
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HOLMES
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PREBLE
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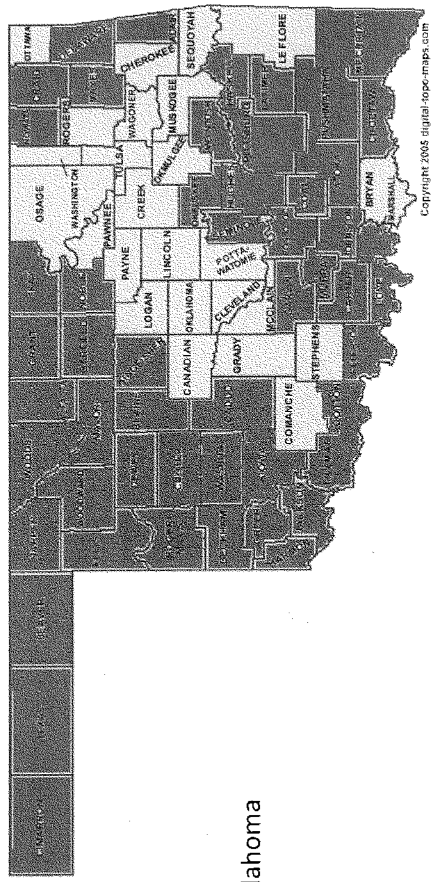
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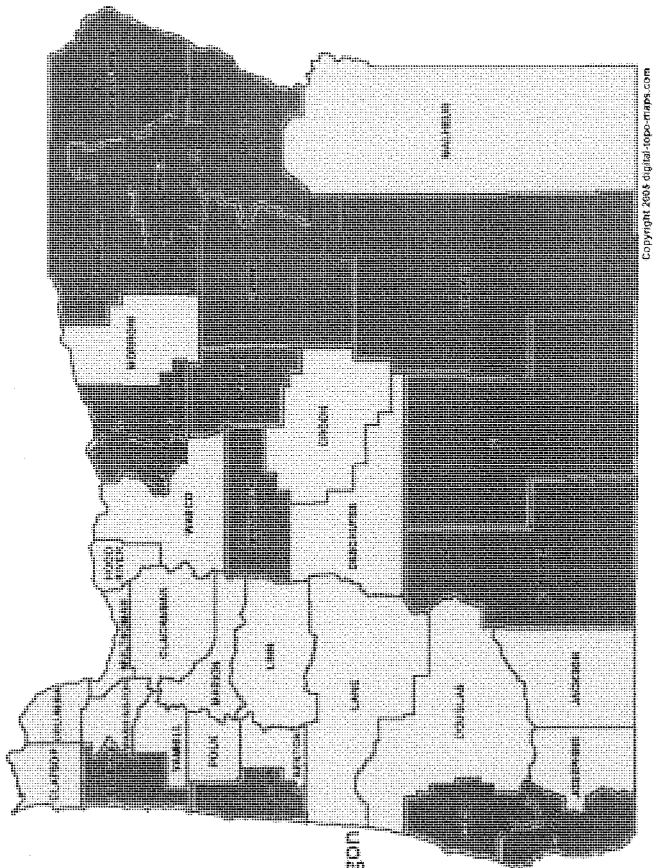

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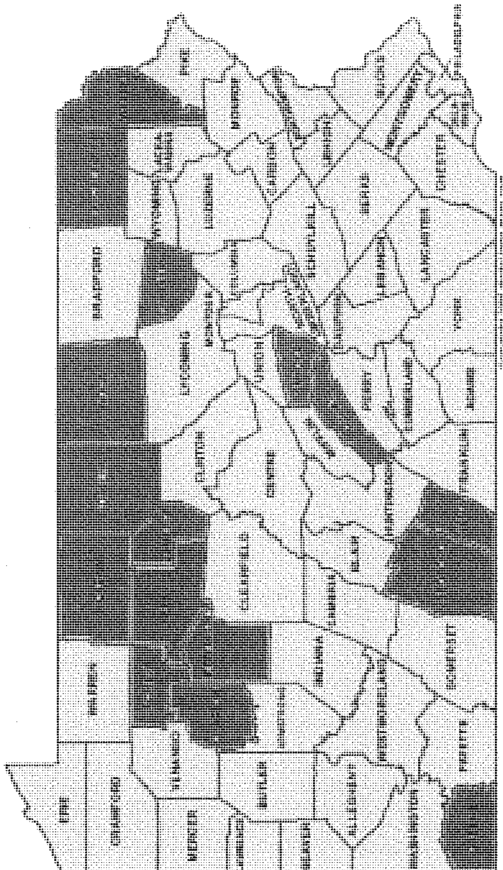

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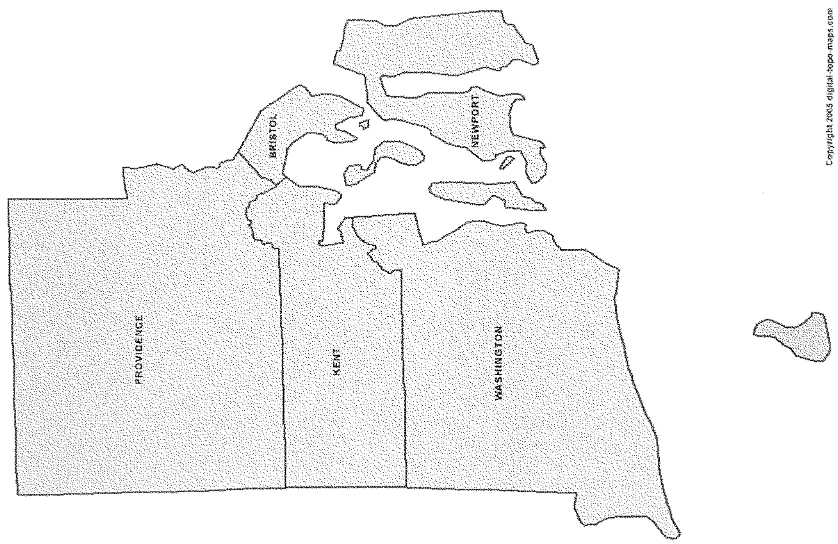

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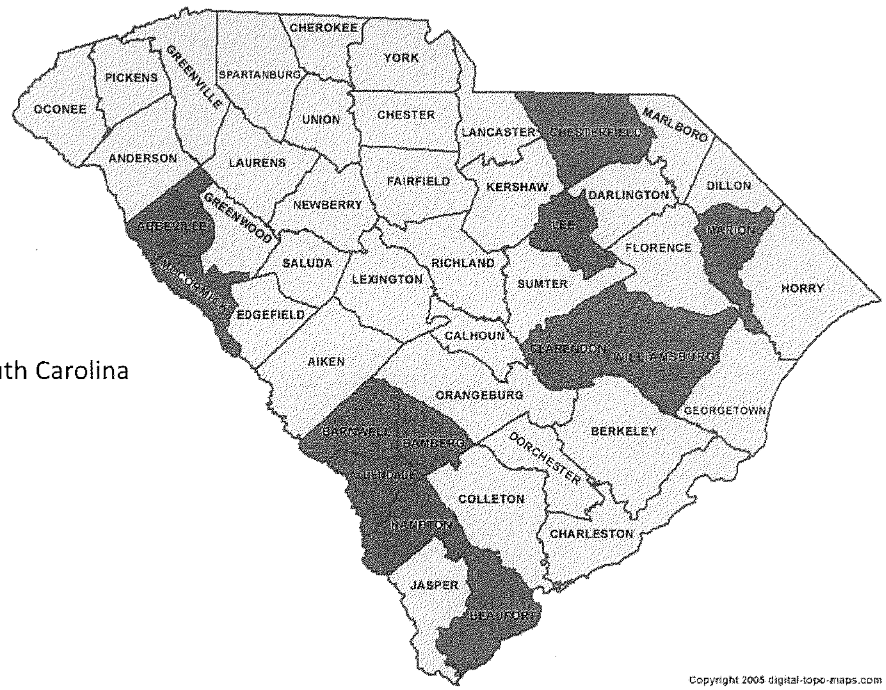

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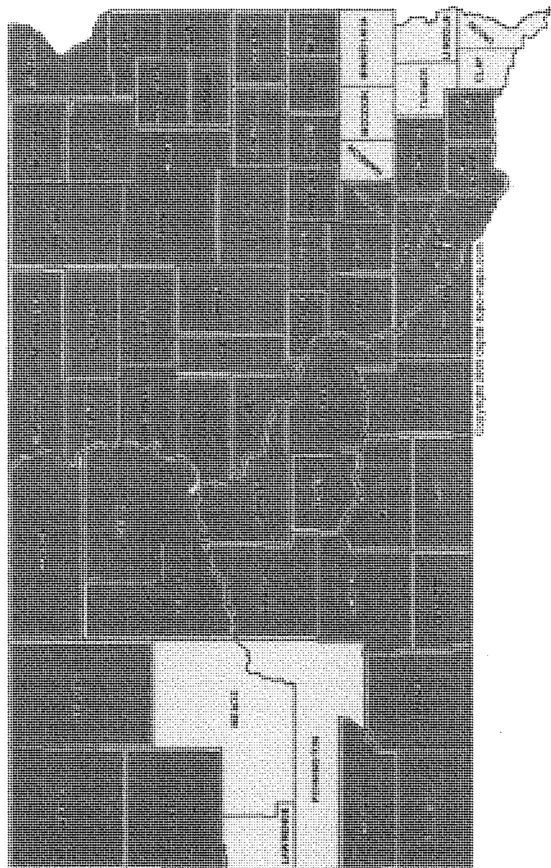

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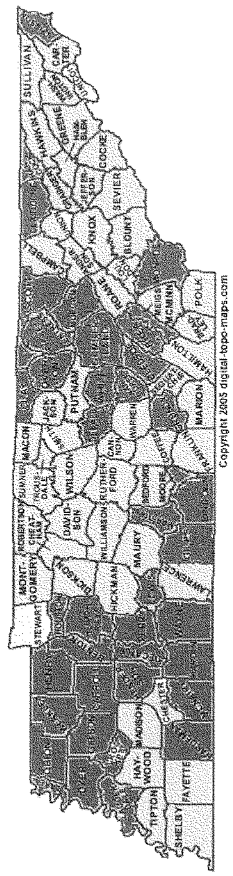
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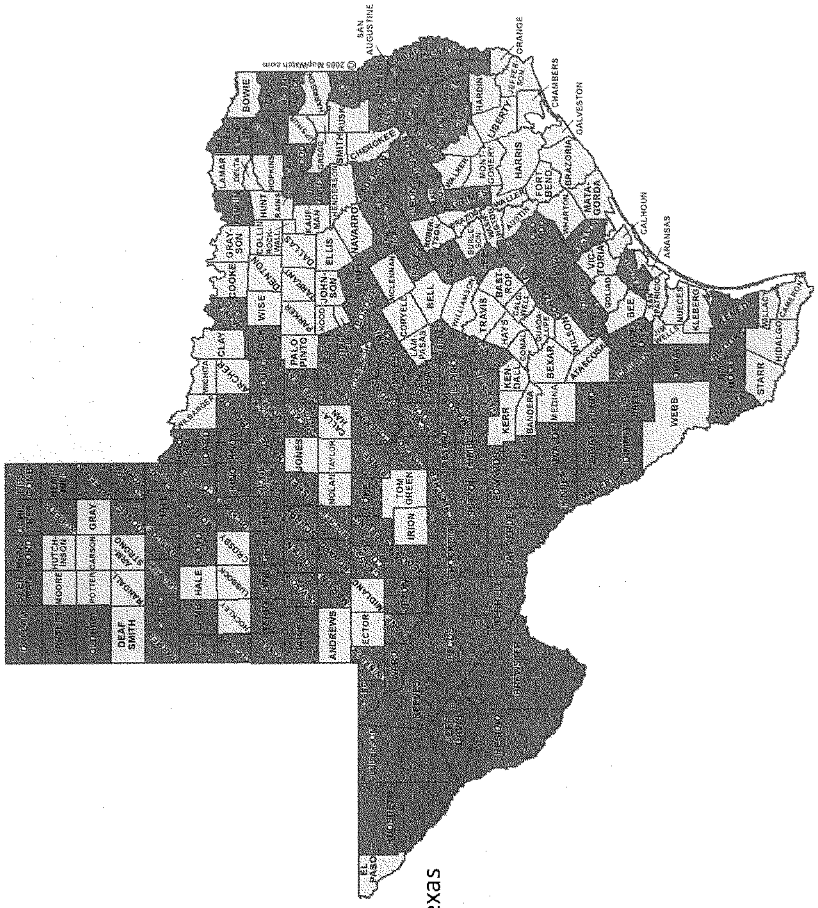
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FORT BEND
BRAZORIA
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KAUFMAN
DALLAS
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TARRANT
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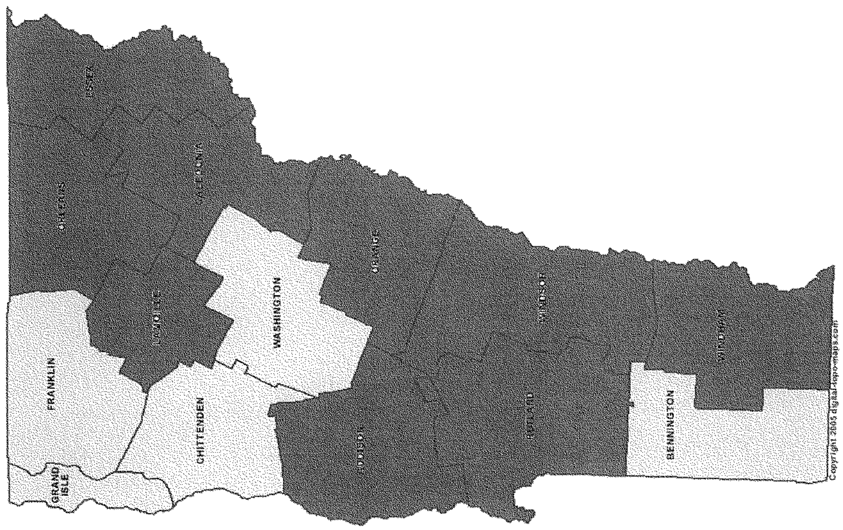
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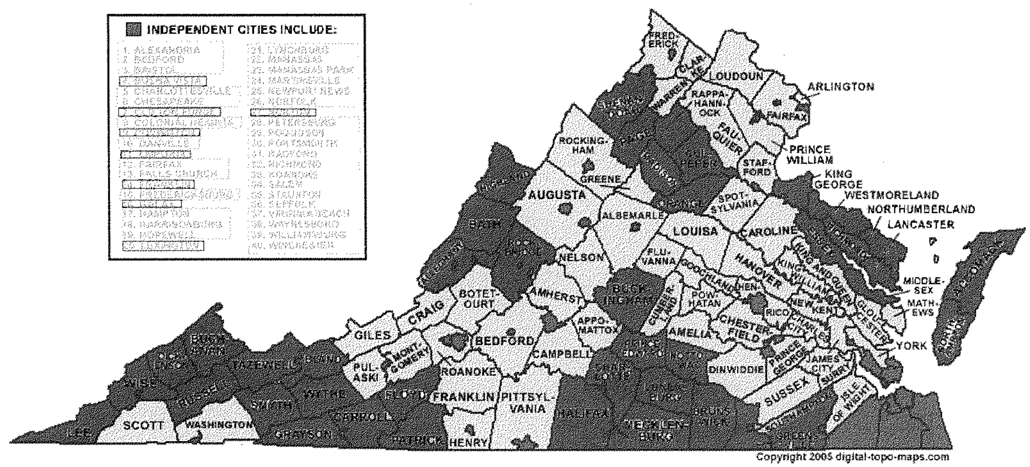
Virginia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STAF-FORD
KING GEORGE
WESTMORELAND
NORTHUMBERLAND
LANCASTER
ROCKING-HAM
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ALBEMARLE
SPOT-SYLVANIA
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GOOCHLAND
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MATH-EWS
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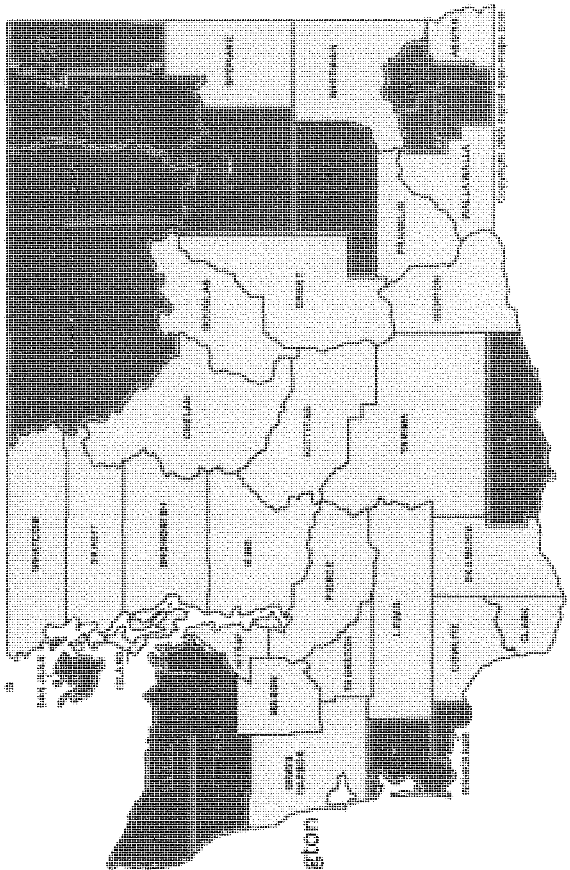

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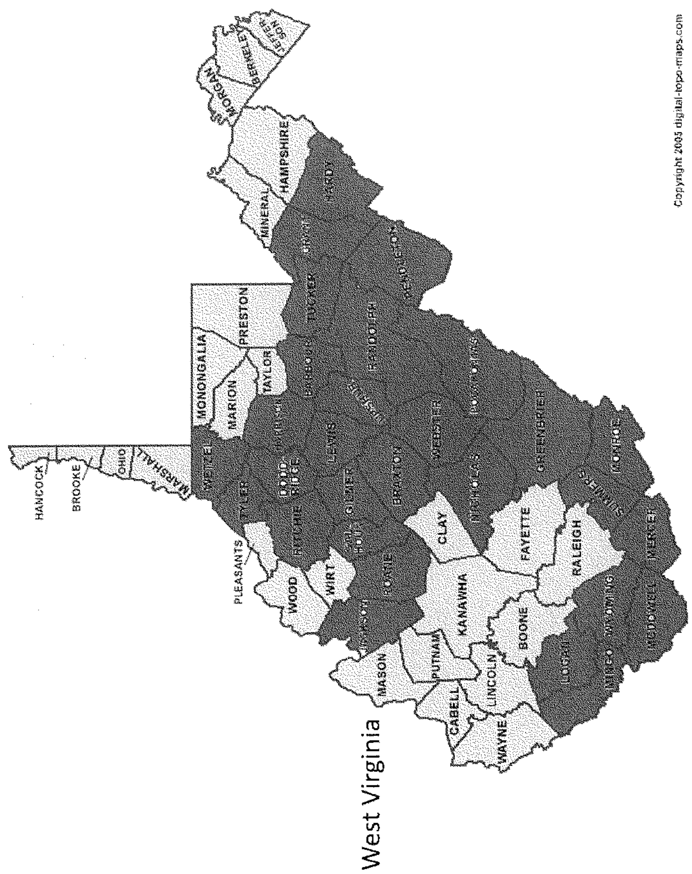
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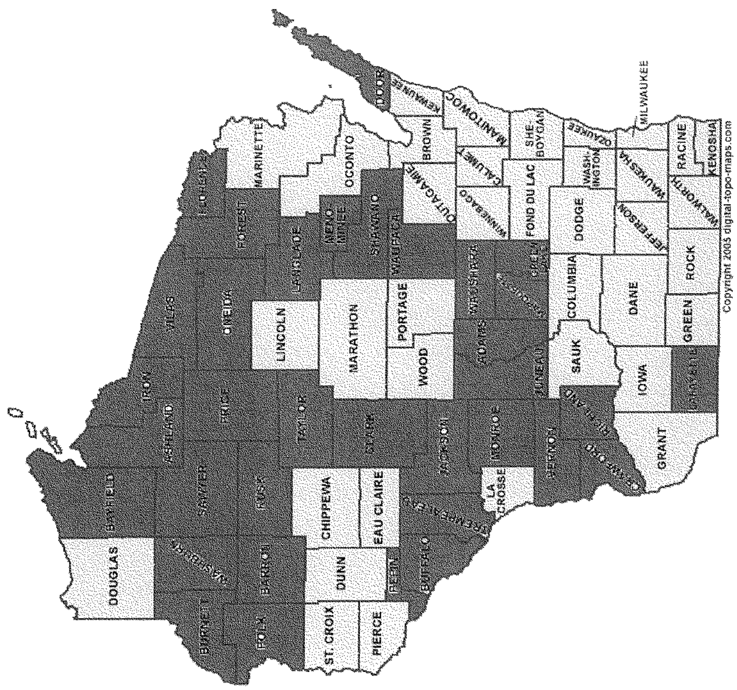
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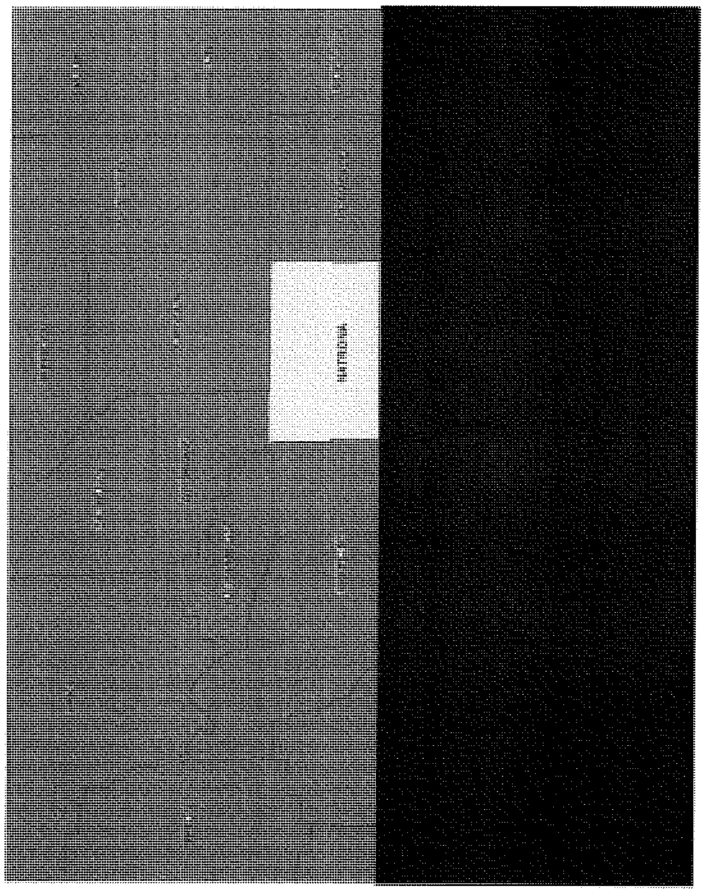

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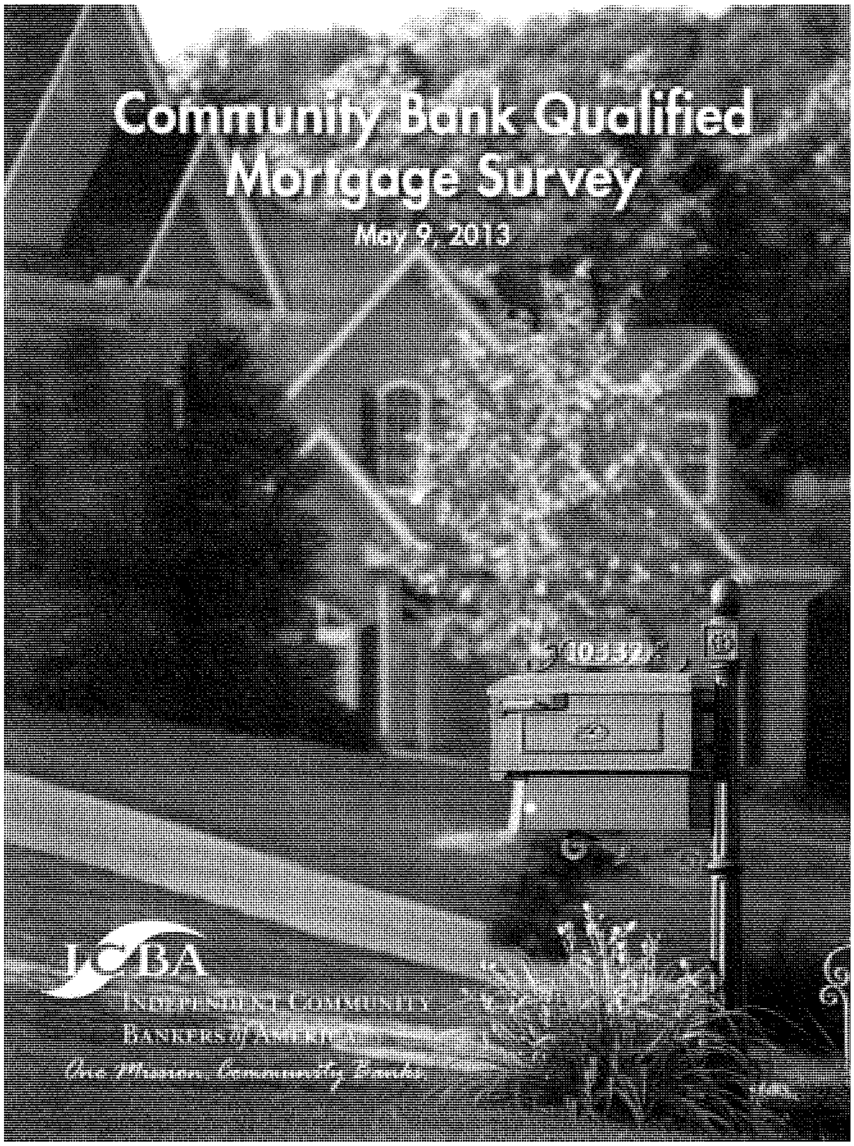
Community Bank Qualified Mortgage Survey
May 9, 2013
ICBA
Independent Community Bankers of America
One Mission. Community Banks.

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Community Bank Qualified Mortgage Survey: Summary of Findings

ICBA conducted a survey to gather data on the impact of the accommodations for community banks in the CFPB's Qualified Mortgage/Ability to Repay rule. ICBA requested information on community banks' residential first-lien mortgage lending activities for 2012.

ICBA distributed the survey to its membership between February 7 and February 14, 2013 and requested that the survey be directed to the member of bank staff best prepared to answer questions on the topic. ICBA received 380 responses, a response rate of approximately 8%.

For the purposes of our analysis, respondent community banks were selected for peer groups based on their responses to questions on their asset size and the geographic areas served.

Key Findings

- **Among the 75% of respondent community banks that currently make balloon mortgages, less than half (46%) would qualify for the balloon mortgage exception to the Qualified Mortgage/Ability to Repay rule.**

- **For respondent community banks that consider themselves to be rural banks, 44% do not qualify as "rural" under the rule's definition.**

- **Among the community banks that do not qualify for the balloon exception, most are disqualified primarily on the basis of the definition of "rural" (43% overall) or limited by a combination of the 500 loan annual originations cap and the definition of "rural" (9% overall).**

- **Among respondent community banks, an overall average of 64% of originated residential mortgage loans are held in the bank's portfolio for the life of the loan. The majority of respondent banks (52%) hold at least 80% or more of the loans originated for the life of the loan.**

- **Only 33% of the respondents originate and hold ARMs in portfolio. Smaller community banks are less likely than average to originate and hold ARMs in portfolio.**

- **Most respondents (64%) indicate they make higher-priced mortgage loans and provide escrow accounts for them (as required by federal regulation).**

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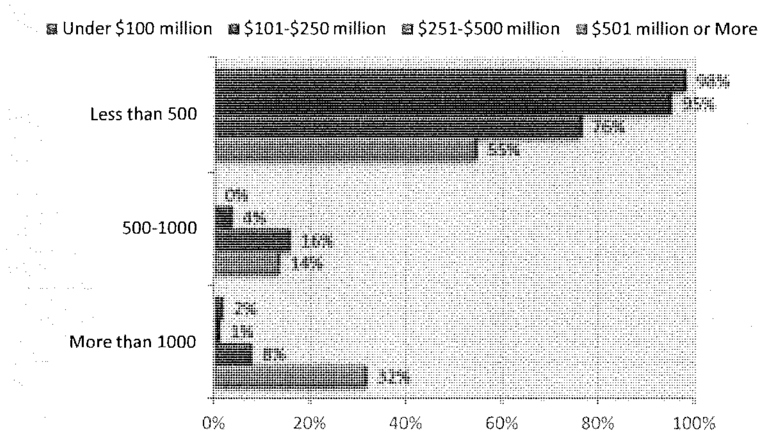
Mortgage Originations

Most of the responding banks (90%) originated fewer than 500 mortgage loans in 2012. Almost all responding banks with less than $100 million in assets did so (98%). Most banks with $101-$250 million in assets originated fewer than 500 mortgages (95%).

While the balloon exception is for banks with up to $2 billion in assets, larger community banks find it more difficult to qualify for the exception based on the number of mortgages originated. Nearly one-fourth (24%) of respondent banks with $251-500 million in assets will be unable to use the balloon exception because they originate more than 500 mortgages. Only 55% of banks with more than $500 million in assets originate fewer than 500 loans, so 45% of banks in this category will be unable to qualify for the balloon exception based on the number of originations (Figure 1).

Figure 1: How many residential first-lien mortgage loans did your bank originate during the calendar year 2012?



Loans Held in Portfolio

Among respondent community banks an overall average of 64% of residential mortgage loans are held in the bank's portfolio for the life of the loan. The majority of respondent banks (52%) hold at least 80% or more of the loans originated for the life of the loan (Figure 2).

Larger community banks hold a smaller percentage of loans in portfolio for the life of the loan. Among respondent banks with more than $250 million in assets, 46% of originated loans are

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held in portfolio for the life of the loan, compared to 65% for banks with $101-250 million and 72% for banks with less than $100 million in assets. Also, rural banks hold a higher percentage of originated loans in portfolio (68%) compared to suburban (53%) or urban (43%) banks (Figure 2). When we examine the data as the percentage of respondents that fall within percentage ranges, the same trends are apparent (Figure 3 & 4).

Figure 2: What percentage of the loans originated in 2012 are to be retained in the bank's portfolio for the life of the loan? - Mean

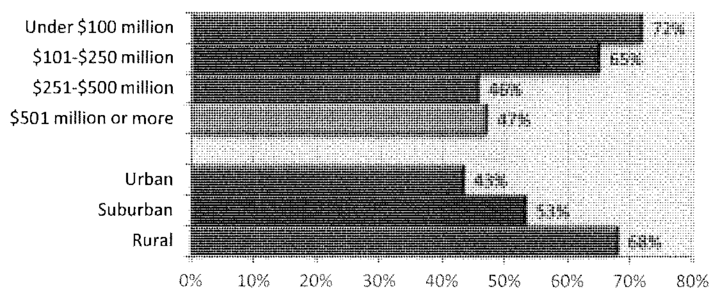

Figure 3: What percentage of the loans originated in 2012 are to be retained in the bank's portfolio for the life of the loan? – Percent within Ranges by Asset Size

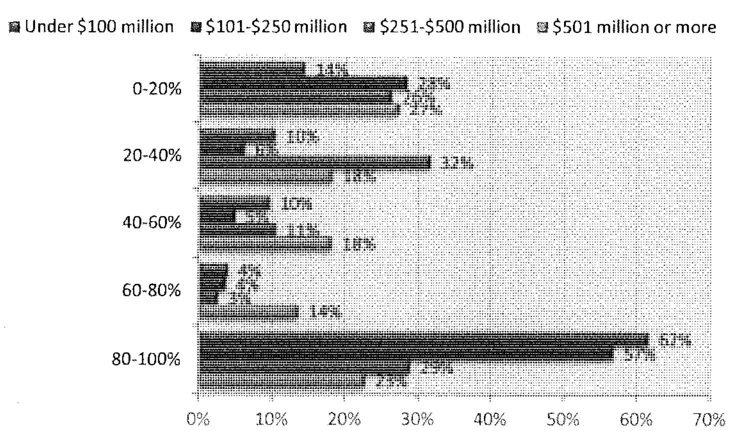

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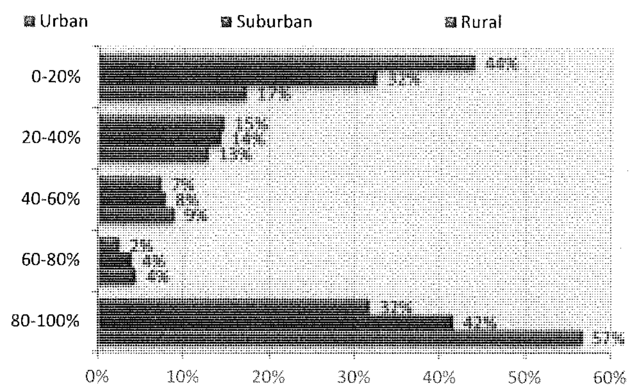
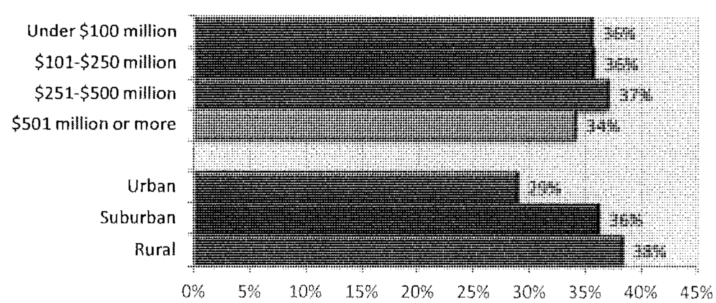
Figure 4: What percentage of the loans originated in 2012 are to be retained in the bank's portfolio for the life of the loan? – Percent within Ranges by Geography



Adjustable Rate Mortgages

Asset size makes little difference to the percentage of adjustable rate mortgages (ARMs) with all peer groups close to the overall average of 36%. However, banks that report serving urban markets made fewer ARMs as a percentage of overall loans than other banks (29%, Figure 5).

Figure 5: What percentage of your bank's residential first-lien mortgage loans held in portfolio have adjustable rates (ARMs)?



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One-third (33%) of respondent banks indicate they have no ARMs in their portfolio and institutions with less than $250 million in assets are even less likely to have ARMS in their portfolio (Figure 6 & 7).

Figure 6: What percentage of your bank's residential first-lien mortgage loans held in portfolio have adjustable rates (ARMs)? – Percent within Ranges by Asset Size

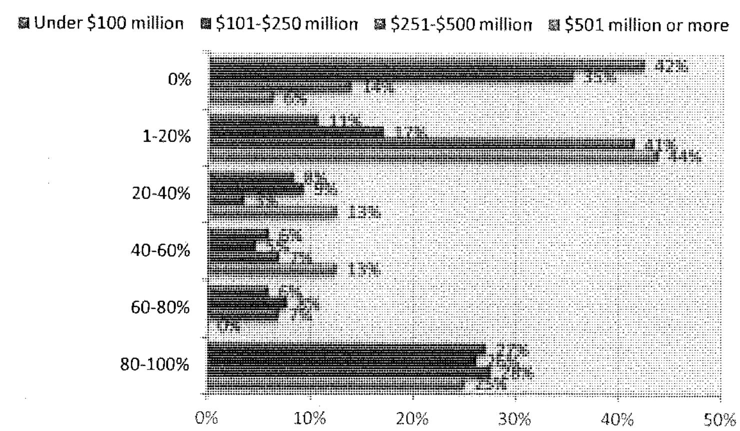
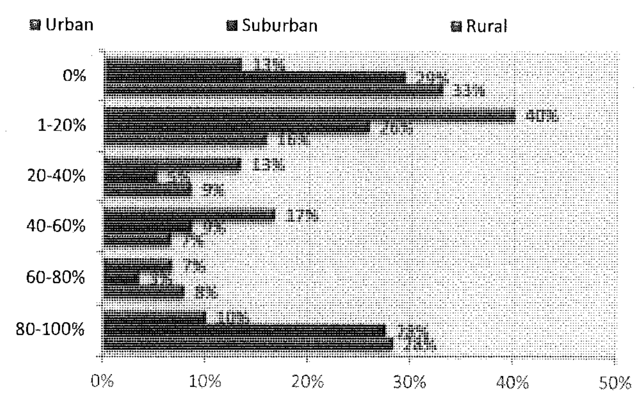


Figure 7: What percentage of your bank's residential first-lien mortgage loans held in portfolio have adjustable rates (ARMs)? – Percent within Ranges by Geography



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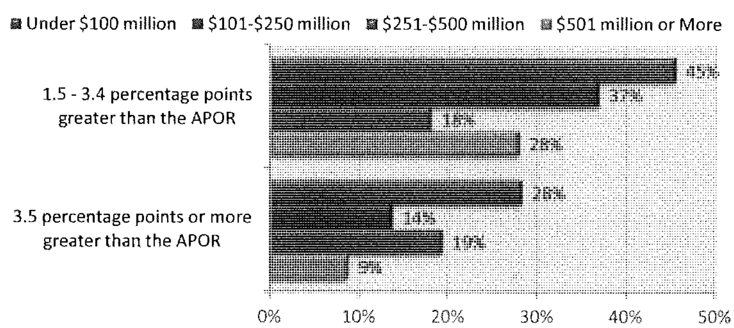
Higher-priced Loans

Bank asset size has a more substantial impact on loan pricing. For respondent banks with less than $100 million in assets, most loans (74%) have an APR that exceeds the APOR by more than 1.5 percentage points. For banks serving rural areas, 62% of loans exceed the APOR by 1.5 percentage points and 22.5% exceed the APOR by more than 3.5 percentage points (Figure 8). This reflects the higher cost of funds and operations for smaller banks and rural banks.

Figure 8: What percentage of residential first-lien mortgage loans originated by your bank have an Annual Percentage Rate (APR) that exceeds the Average Prime Offer Rate (APOR) for mortgage by the following amounts?



Most respondents (64%) indicate they make higher-priced mortgage loans and provide escrow accounts for them (as required by federal regulation, Figure 9). Fewer banks with less than $100 million in assets provide escrow accounts, with one-third (33%) indicating they do not provide higher-priced loans because they cannot or choose not to satisfy the escrow requirements.

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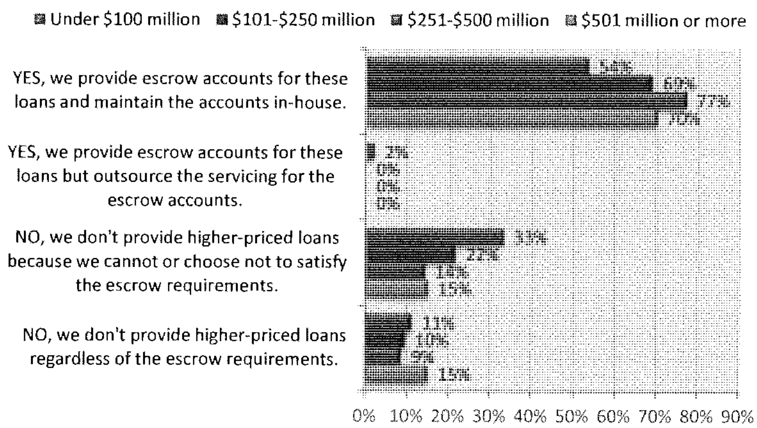
Figure 9: Does your bank currently provide escrow accounts for loans deemed to be higher-priced mortgage loans?



Most respondents (62%) have had a borrower request an escrow account, with institutions with more than $250 million in assets being more likely to have had such a request (more than 80%). The majority of respondents (55%) provided at least one escrow account at the borrower's request during 2012, but most often less than five (24%).

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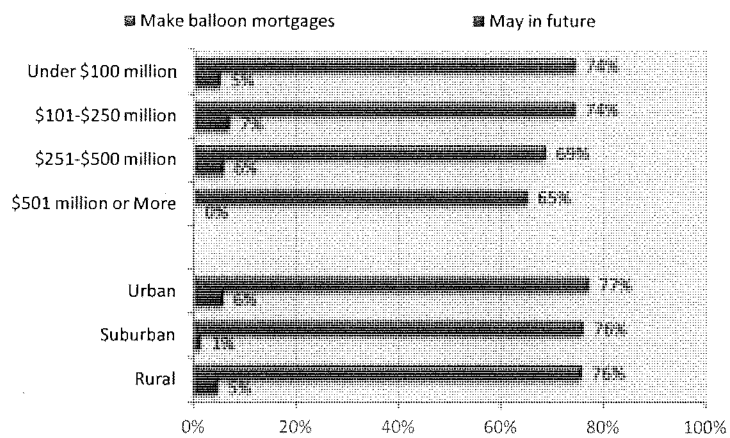
Balloon Mortgages

Most respondents (73%), including a majority of banks in all peer groups, currently make balloon mortgages. Many that do not currently make balloon loans may do so in the future (5%). Smaller banks are more likely to currently make balloon mortgages (Figure 10).

Figure 10: Does your bank currently offer balloon mortgages?



Among survey respondents that currently make balloon mortgages less than half (46%) of community banks would qualify for the balloon mortgage exception. Approximately half of community banks with less than $100 million in assets, between $101-$250 million in assets and indicating that they serve rural areas would qualify (Figure 11). Few larger community banks would qualify, including only one-in-three (33%) of community banks with $251-$500 million in assets and one-in-twelve (8%) community banks with more than $501 million in assets would qualify.

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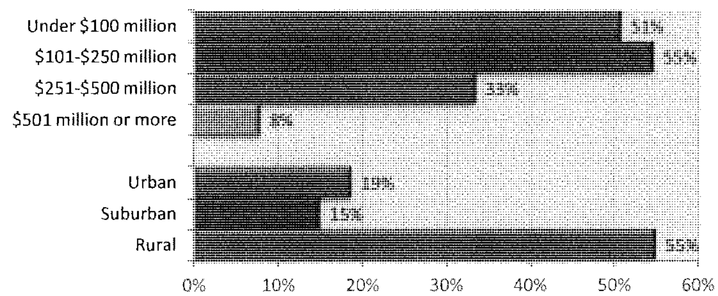
Figure 11: Percentage of Community Banks Qualifying for Balloon Mortgage Exception by Peer Group



Community banks that do not qualify for the exception are disqualified primarily on the basis of the definition of "rural" (43% overall) or a combination of the number of originations and the definition of rural (9% overall). Only 1% of banks are disqualified based solely on the number of originations.

Most banks with less than $250 million in assets that currently make balloon mortgages but would be unable to qualify for the exception are disqualified by the definition of rural. Larger banks with more than $250 million in assets are likely to be disqualified by both the number of originations and the definition of rural (Figure 12). Given the impact of these factors the $2 billion asset cut-off has little meaning, and few community banks with $501 million - $2 billion in assets will qualify for the balloon exception.

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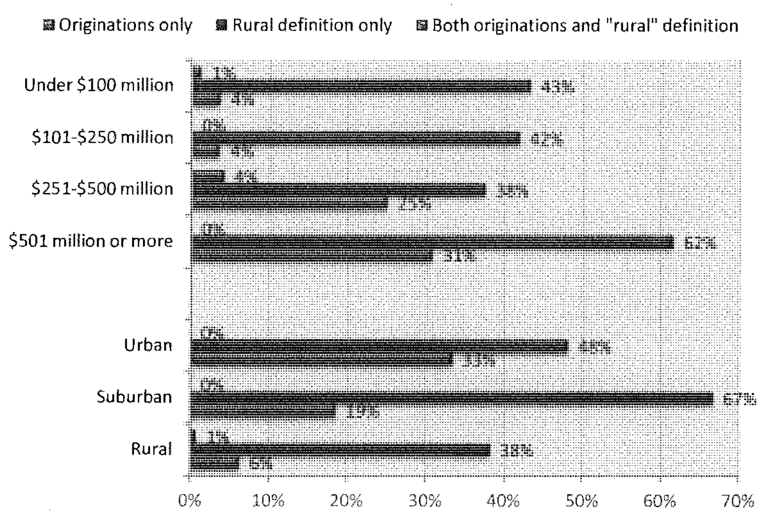
Figure 12: Percentage of Community Banks Disqualified for Balloon Mortgage Exception by Qualifying Factor



Qualifying under the Rural Definition

Most small and rural banks originate loans in only one or a handful of counties, with 92% of banks with less than $100 million in assets serving 5 or fewer counties and 98% of banks in this size category serving 10 or fewer counties. For rural banks, 72% serve 5 or fewer counties and 90.5% serve 10 or fewer counties.

Overall, fewer than half of respondent banks (47%) indicate they make more than 50% of mortgage originations in qualifying counties in neither a metropolitan statistical area (MSA) nor an adjacent micropolitan statistical area under the definition of rural in the Ability-to-Repay/Qualified Mortgage rule.

Significantly, among banks that indicate they serve rural areas, 56% make more than 50% of their mortgage loans in qualifying counties – that means 44% of respondent rural banks will not meet the standard of "rural" in the QM rule. Only 5% of respondent banks with more than $500 million in assets indicate that they will meet this requirement (Figure 13).

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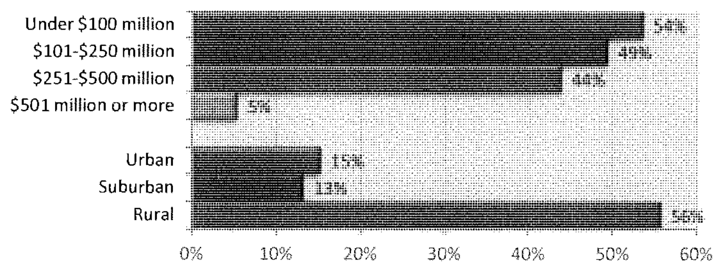
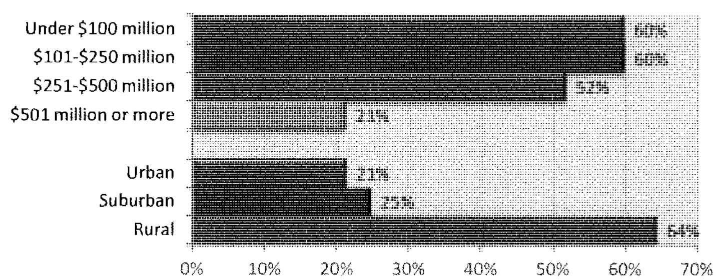
Figure 13: Does your bank provide over 50% of its residential first-lien mortgage loans in counties that are neither in a metropolitan statistical area (MSA) nor in a micropolitan statistical area adjacent to an MSA? - Yes Responses



If the definition of rural were expanded to include all counties outside MSAs, more banks would qualify as rural, including 21% of banks with more than $500 million in assets. However, banks serving urban and suburban markets in addition to rural markets will continue to find it difficult to qualify for the exemption.[1] And 36% of banks that characterize themselves as rural still would not meet the QM definition of rural (Figure 14).

Figure 14: Does your bank provide over 50% of its residential first-lien mortgage loans in counties that are outside an MSA (even if some are in micropolitan counties)? - Yes Responses



[1] Among banks serving rural areas, 11% indicate they also serve urban areas and 19% indicate they also serve suburban areas. This degree of overlap is slightly higher than previous ICBA surveys, including the 2012 ICBA Community Bank Overdraft Study (7% and 18% respectively) and the 2011 Community Bank Payments Survey (9% and 18%, respectively).

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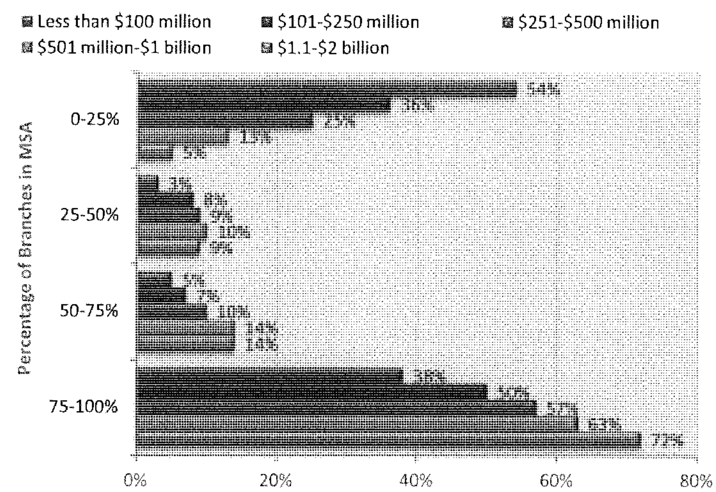
The majority of banks of all asset size groups except those with less than $100 million in assets have most of the branches located inside an MSA (Figure 15).

Figure 15: Percentage of Branches Located in MSA from FDIC Summary of Deposits 2011



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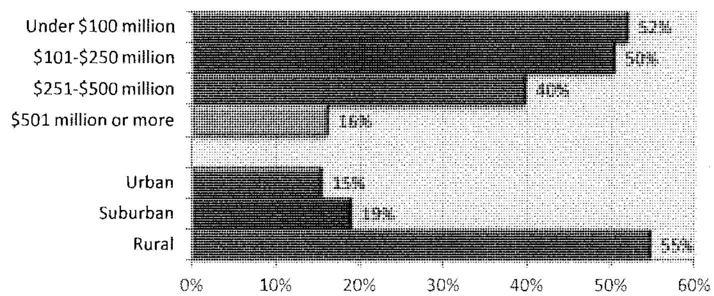
Detailed Data on Mortgage Lending in Rural Areas

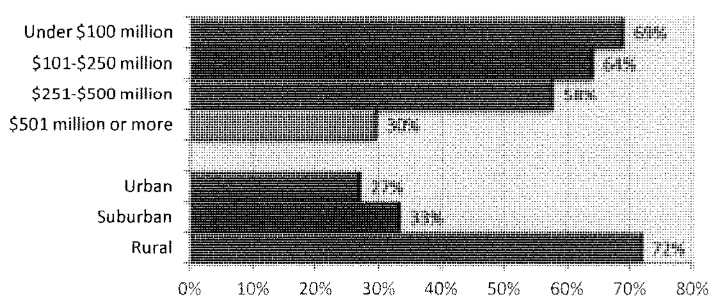
Banks with under $100 million and $101-250 million in assets originate an average of half of their mortgage loans in qualifying counties that are in neither an MSA nor an adjacent Micropolitan Statistical Area (52% and 50% respectively, Figure 16).

Figure 16: What percentage of the residential first-lien mortgage loans originated in 2012 were located in counties meeting the following description? Neither in MSA nor in Adjacent Micropolitan - Mean



Banks with less than $500 million in assets originate an average of more than 50% of their mortgage loans outside of MSAs (Figure 17).

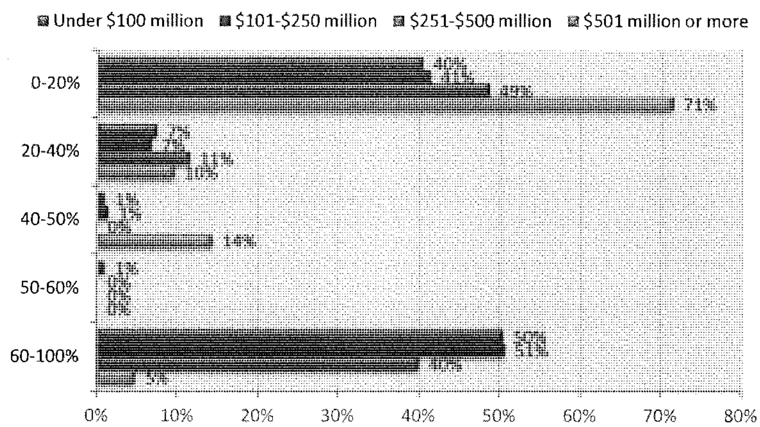
Figure 17: What percentage of the residential first-lien mortgage loans originated in 2012 were located in counties meeting the following description? Not in MSA - Mean



However, 47% of banks with less than $100 million in assets and 48% of those with $101-250 million in assets originate fewer than 40% of their loans in qualifying counties. For banks with $251-500 million in assets, 60% originate less than 40% of mortgage loans in qualifying counties

(Figure 18). This means most banks larger than $250 million in assets will not qualify under the structure of the current definition, even if the threshold is shifted significantly.

Figure 18: What percentage of the residential first-lien mortgage loans originated in 2012 were located in counties meeting the following description? Neither in MSA nor in adjacent micropolitan - Percent within ranges



Few community banks with more than $500 million in assets will meet the 50% standard, with only 5% making more than 50% of mortgage loans in qualifying counties. An additional 14% of banks with more than $500 million in assets make between 40-50% of their mortgage loans in qualifying counties.

Including Micropolitan Statistical Areas adjacent to MSAs in the definition of rural might be expected to increase the number of banks that qualify for the exception; however, the impact is limited. While the average percentage of mortgages originated outside MSAs is below 50% for all assets size peer groups under $500 million in assets, when respondents are grouped into ranges, few banks fall near the threshold (Figure 19).

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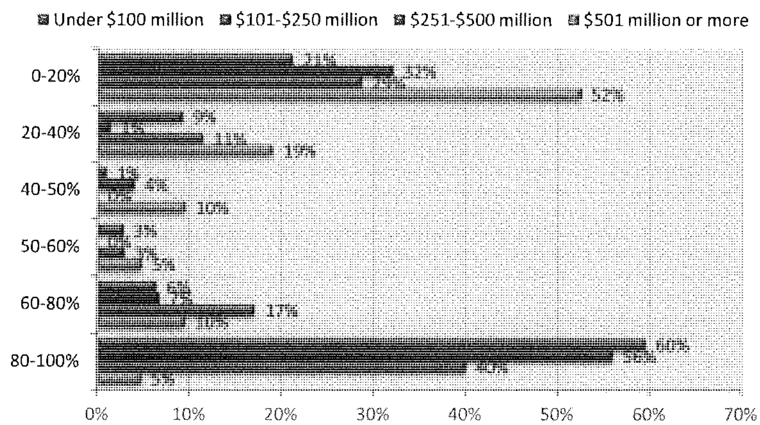
Figure 19: What percentage of the residential first-lien mortgage loans originated in 2012 were located in counties meeting the following description? Not in MSA - Percent within Ranges



Balloon Lending Alternatives

Some banks would consider providing ARMs as an alternative to balloon loans (36%) or increasing ARM lending (29%). However 19% of respondents indicate they would greatly limit mortgage lending or exit the business altogether if restrictions on balloon lending become too burdensome, with the impact greatest among banks with less than $100 million in assets (34%) and those serving rural areas (21%, Figure 20-21).

Figure 20: If federal restrictions on balloon mortgage loans became too burdensome would your bank ever consider providing ARMs as an alternative? By Asset Size

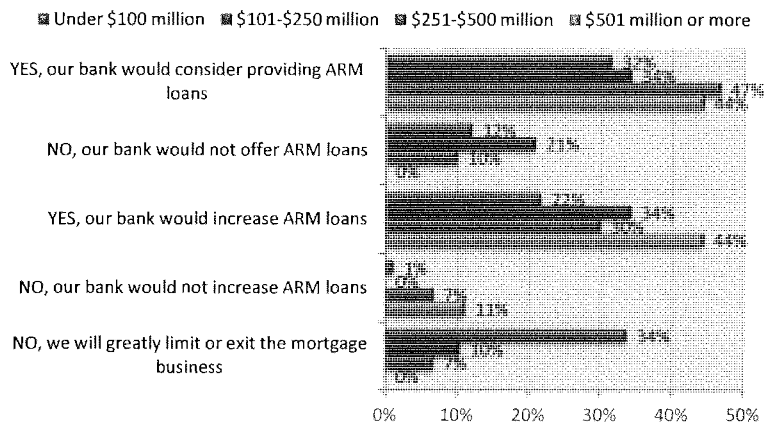
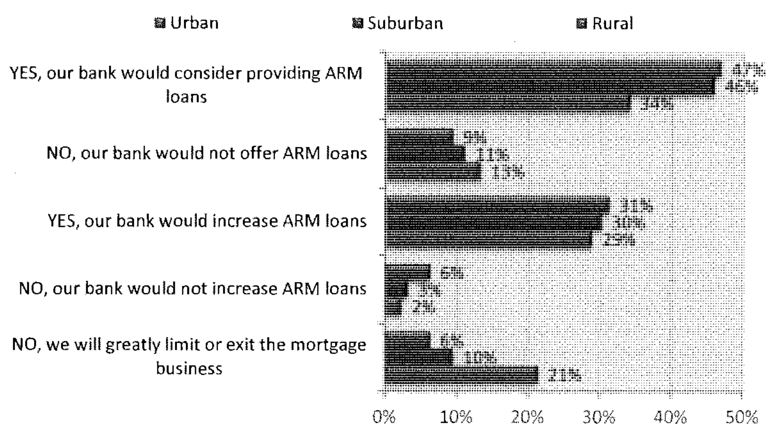


Figure 21: If federal restrictions on balloon mortgage loans became too burdensome would your bank ever consider providing ARMs as an alternative? By Geography



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Appendix A: Selected Banker Text Responses

We have one bank location in Sauk Centre, MN with a population of 4,300 but are pulled into an MSA area for Stearns County because St. Cloud, MN is located 45 miles away. We are as rural as it gets, but not per MSA's standards. We only have 3 stoplights, tractors drive down main street and we are surrounded by farm land - how much more rural can you get? Thank you.

Due to the government purchasing mortgage backed securities in order to drive the rate down, the only mortgage applications we get are for borrowers/properties which don't qualify for the secondary market. We are too small to escrow, therefore we have to do these higher risk loans at a low rate according to the government table. If any more restrictions and/or requirements are jammed down our throats by the government we will stop doing mortgage loans and as the balloons come due we will call the loans and foreclose if they can't pay them in full. Tell me how this will help the customer?

We provide a good mortgage borrowing option for all of our customers that cannot qualify for fixed rate secondary market borrowing. These loans balloon periodically and are always made and maintained at market rates. These are our bread and butter customers that come into the bank every month. We need them to survive as a smaller independent community bank. We are not out to take advantage of the customers we rely on for our existence.

Our bank is located on the far eastern edge (four miles from the county line) in McLean County, IL, the largest county in land area in the state of Illinois. To the east is Ford County, an almost entirely rural county. McLean County contains Bloomington/Normal, a two city community of 100,000 plus population. The several small towns in the rest of McLean county have populations of 2,000 or less. The entire county is considered a MSA, due to Bloomington/Normal. Our bank is located in Anchor, a town of 150 population in a rural area, about 25 miles east of Bloomington/Normal, but unfortunately still in McLean County.

Up until the recent change in regulations, our bank made three, five, and seven year residential balloon loans to low and moderate income residents of Anchor, surrounding rural areas, and neighboring small towns. Most of these loans were less than $100,000 (many $50,000 or less) and were not of much interest to large institutions. [All the larger "prime" loans went to larger institutions in Bloomington/Normal who are active in the secondary market.]

We kept all loans in our in-house portfolio and did our own loan servicing. We never had any difficulty with arranging extensions/modifications with customers who reached a balloon maturity. With a small staff of three full time employees (including me) we did not feel we could afford the extra expense of escrow accounting and compliance. With the increasing complications of lending under the HOEPA and higher-priced mortgage regulation we felt forced to discontinue residential real estate lending (except for rental properties) in 2010. Prior to the regulation changes, if a residential loan customer asked about escrow, we offered to set up a separate savings account and make monthly transfers from their checking of 1/12th the amount needed to pay real estate taxes and homeowner's insurance. It was up to the customer to make sure they took out the money and paid their taxes and insurance when they were due. This arrangement has worked fine since I came to the bank in 1979.

While it may not be politically correct to say it, our first duty as bankers is to make a profit for our shareholders. If we do not, the bank is not here to serve our community. We would like to resume small

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residential real estate lending. Our customers want it and it would help our profitability. BUT, it appears the proposed regulations will require us to do formal escrows (with the accompanying accounting and compliance burdens), even though we are located 25 miles from the large community which lands our county in the MSA classification. Please feel free to contact me if you need additional information or elaboration.
An arbitrary floor of $2 billion is not sufficient for Banks in Montana. It is a large state with low population, and this level would exclude our two largest institutions ($7B in size). These two institutions still serve a great portion of Montana - much of which is rural. We need a consistent floor applied across the regulations.
We used to offer balloon mortgages before all the changes several years ago. It served our bank and our market very well. We started up our escrow accounts out of necessity to meet regulations not because we or our customers wanted them. I hope CFPB will pay attention to this.
1) The vast majority of our residential mortgage are "outside the box" of one or more secondary market guidelines (acreage, mixed use, D/I ratios, etc.) 2) 20% down (or equity on refinances) is required on all residential mortgage loans. 3) In our 100+ year history, the Bank has never initiated foreclosure on any residential mortgage loan.
The proposed CFPB regulations may well drive us out of residential mortgage lending
The balloon loans that we are making are to consumers who otherwise would not be eligible for mortgage credit for various reasons. We are taking additional risk by making these loans and we provide a valuable service to our customers by doing so. I know that we are considered to be in an MSA but we are very rural and I don't think we should be subjected to the new rules. Sometimes the current appraisal underwriting guidelines create a lot of problems for borrowers because of the lack of sales of similar type properties because we are so rural. We end up having to find other alternatives to Freddie and Fannie. That includes booking loans on our books instead of selling them.
We just started escrow services this month in anticipation of the new HPML rules. We have one loan on the books that has escrow that we booked this month. We have always originated balloon loans. We would prefer not to offer ARM loans but that may be a necessity.
The current HPML regulations are extremely burdensome on our staff & also confusing for the average customer. Most customers do not understand why we have to escrow, why we give them some of these disclosures, or why they have to wait so long to close their loan. As we are forced to escrow more & more loans, it may become necessary for our bank to hire one or two more employees to keep up with this regulation alone. That's a huge expense for a bank our size!
Our little bank was forced by regulations to offer escrow on mortgage loans starting in April 2010. However, not all counties in our area will send tax bills to the bank which causes confusion for our customers. Of course, I'm still curious how the lack of escrow on a mortgage loan contributed to the mortgage crisis caused by poor underwriting.

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Our bank will not make a loan that would be classified as a higher-priced mortgage due to the additional regulatory burden required by these mortgages including escrow requirements. Requests that would result in a Higher-priced Mortgage are either modified or we simply refuse to make the loan.
Most of our current business is very rural, but we have a growing presence in a MSA. I think the rule should not apply to loans made out of the MSA even if we go over 50%. In January of 2013 2/3s of our loans were made in the MSA.
If the definition of urban includes a micropolitan county then our bank is going to have serious problems. We operate in Randolph County, Missouri which has an approximate population of 25,000. To consider us anything other than rural is absurd.
We have a major rural presence but the rural balloon loan option is not open to us because we are over the $2 Billion threshold. The qualifying standard should be changed to more accurately address the lending needs community banks serve in rural areas. Balloon loans should be allowed in rural areas regardless of bank's size. Forcing banks back into ARM loans may present even larger problems down the road.
We are located in rural southern Carlton County, MN which is included in the Duluth MSA which makes no sense. 1.5% over the APOR & 3.5% for 2nd REMs. How are we supposed to make payroll, maintain capital and get any ROE? Where do theses APOR's come from? FANNIE & FREDDIE? Is that really fair considering their source of funding & ours? If they need to cover losses they fire up the printing press. Our regulators would just padlock our door being we're not "too big to fail". Sorry I had to vent a little. Thanks for doing this survey. I hope the Feds will turn up their hearing aids and get a grip on reality.
The new requirements for required escrows are a burden to our staff. We are a small community bank.
You are absolutely correct that rural has been defined too narrowly and will keep the majority of banks from qualifying.
There should be NO connection between "high priced" mortgage loans and Mandatory Escrow Accounts. With all of the regulations requiring escrow accounts, it is prohibitive for small community banks to offer them.
Our bank began offering escrow accounts in 2012, so the APR's on our mortgages will likely increase in the future. The only mortgages we offer have balloon features because we service our loans and cannot risk long term fixed rates. The vast majority of our mortgage borrowers would not qualify for 15 - 30 year, fixed, low rate loans. Their default risk is higher, therefore, requiring a higher interest rate. Otherwise, these potential home owners will have to continue renting.
Our bank has not foreclosed on a residential mortgage during the past 15 years and perhaps only 2 homes during the preceding 10 years. We have never refused to renew a balloon payment loan at its maturity. The renewal process is a beneficial opportunity to meet with borrowers and advise them on debt structure and financial progress.

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We are a small community bank located in Houston County, Minnesota with the City of LaCrosse, WI located across the river (the real MSA). We are totally NOT a metropolitan area. We have an ag concentration with approximately 80% of our loan portfolio in ag related loans. We do in-house balloon loans for borrowers who do not qualify for a secondary market loan due to a ding in their underwriting (approximately 10% of our portfolio). None of the balloon loans are over 30 days delinquent. We will discontinue offering in-house loans if we cannot offer balloon loans. We are considering discontinuing loans not qualifying for the secondary market already, due to required escrow accounts, which we do not offer. Rates on this type of loan do not reflect risk, due to limiting the interest rate by not offering escrow accounts.
It is the bank's policy to require escrow's on all 1st mortgage residential loans. We do get about 3% requests for exclusion.
We agree that rural is too narrowly defined, and that once again we find a regulation intended to help the consumer that will actually prevent the consumer from getting financing.
Even though we belong to the St. Louis MSA, we are in a very rural area. We are the only bank in 2 of the 4 towns we have branches in. We are an hour from the suburban area.
Our bank has 2 offices located in the eastern, rural portion of Pottawattamie County, IA (which is part of the Omaha/CB MSA), so, even though we are certainly in a "rural" farming area, and the population of our 2 communities is less than 1,400 people, we are explicitly excluded from the "rural" exemption due to a large city located in our county, approx 20 mi away. Our bank has 10 employees covering 2 offices. We have 3 loan officers, one of which is our only mortgage loan officer - in other words, we have a mortgage department of "1". Due to staggering regulatory burden placed on community banks during the recent mortgage reform, our bank has had to stop offering consumer owner-occupied loans. Recent mortgage revisions and prohibitions have made mortgage lending not only impractical, but impossible for a small community bank such as ours.
We have been doing ARM loans and escrowing taxes and insurance for years. We portfolio all of our loans.
We are a small community bank, but we regularly do more than 500 first mortgage originations per year. We believe that this number should be increased for the exemption. We also think that the 43% maximum on the debt-to-income is too restrictive to self-employed borrowers along with S-corp. or sole proprietors.
The margin of 1.5% over the APOR needs to be increased to at least 3.5%. Our bank cost of funds is not the same and is higher than a national cost of funds or the Mega Bank cost of funds on which the APOR is based. Since we hold 100% of our originations in portfolio, we need to be able to price off our internal cost of funds. If we sold into the secondary market the 1.5% margin would be OK, but since we are a portfolio lender, staying under the 1.5% margin squeezes our NIM and if we exceed the 1.5% the escrow requirement makes our cost to service our limited number of loans too high. In 2012 the bank originated 31 1-4 family first lien loans in our small rural community that is located within the Waco Texas MSA. The regulation as currently written by the CFPB will have a substantial negative impact on our bank.

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We currently do not fall in the exception because only 43% of our loan originated fall within the definition of rural/underserved. Many of these counties are located adjacent to a metro area; however, clearly should be considered rural or underserved. I think the rural underserved classification should be re-examined.
Please remember that most of our customers that have portfolio loans are low income and purchase the lower dollar houses. The secondary market is not interested in these low dollar houses. If it becomes too burdensome to provide portfolio loans and the bank restricts or stops providing these loans it will truly hurt the low income people. One must remember that portfolio loans generally have very low closing costs which help low income people to get into the house in the first place.
Most loans are HPML and balloon. We offer no ARM's now and only started escrow to try to service the mortgage need in our community for those loans not qualifying for the secondary market because of appraisal issues, acreages, sole proprietorship needing income verification, time in job, etc. We want to make mortgage loans to our customer base, but it is becoming extremely difficult and expensive to be compliant. We have a strong history and virtually no delinquencies but are being overpowered by compliance regulation.

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June 17, 2013

The Honorable Shelley Moore Capito Chairman Subcommittee on Financial Institutions and Consumer Credit House Financial Services Committee United States House of Representatives Washington, D.C. 20515	The Honorable Gregory Meeks Ranking Member Subcommittee on Financial Institutions and Consumer Credit House Financial Services Committee United States House of Representatives Washington, D.C. 20515

Re: Credit Union concerns with the CFPB's Qualified Mortgage ("QM") Rule

Dear Chairman Capito and Ranking Member ~~Meeks:~~ Chairman Capito

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents the interests of our nation's federal credit unions, I write today in conjunction with tomorrow's hearing, "Examining How the Dodd-Frank Act Hampers Home Ownership." NAFCU member credit unions and their 95 million member-owners appreciate the subcommittee's continued focus on the complex Qualified Mortgage ("QM") final rule scheduled to take effect in January of 2014.

As members of the subcommittee are aware, a host of mortgage related rules are currently being promulgated. These rules, taken individually or in their cumulative effect, will undoubtedly alter the mortgage market in unintended ways. The ability-to-pay rule is of particular concern moving forward as the stringent requirements contained in the final rule will greatly affect credit unions' mortgage lending policies as well as their mortgage operations. Accordingly, in a recent survey of NAFCU member credit unions, nearly 44% of respondents said they will cease originations of non-qualified mortgages (QM). Another 44% indicated they will reduce originations that fall outside of the QM guidelines.

NAFCU has taken advantage of every opportunity available to educate and weigh in with the Consumer Financial Protection Bureau (CFPB) on aspects of the ability-to-repay rule that are likely to be problematic for credit unions and their members. While credit unions understand the intention of the rule and importance of hindering unscrupulous mortgage lenders from entering the marketplace, we cannot support the ability-to-repay rule in its current form. A major issue, for example, is the underwriting criteria that dictates a consumer have a total debt-to-income (DTI) ratio that is less than or equal to 43 percent in order for that loan to be considered a QM. NAFCU believes this arbitrary threshold will prevent otherwise healthy borrowers from obtaining mortgage loans and will have a particularly serious impact in rural and underserved areas where consumers have a limited number of options. In addition, as the subcommittee is aware, the rule excludes from the definition of QM those mortgage loans with terms exceeding 30 years. By definition this punishes credit unions and their members if a longer-term product is the best choice under a particular set of certain circumstances.

Simply put, the DTI requirement is too restrictive and would effectively exclude many otherwise creditworthy consumers from the mortgage market. The requirement also does not take into account a number of factors that are relevant in determining a consumer's ability to repay, including debt that will be paid within a short period of time or likely increases to income, such as through inheritance. We believe that the CFPB should either remove or increase the DTI requirement on qualified mortgages.

Additionally, before the ability-to-repay rule goes into effect, we also urge the subcommittee to review and address the definition of "points and fees" contained in the rule. As currently defined, "points and fees" will include, among other charges, fees paid to affiliated title companies, amounts of insurance and taxes held in escrow, loan level price adjustments, and payments by lenders to correspondent banks, credit unions and mortgage brokers in wholesale transactions. As a result of this troublesome definition, many affiliated loans, particularly those made to low- and moderate-income borrowers, would not qualify as QMs and would unlikely be made or would only be available at higher rates. NAFCU supports Rep. Huizenga's bipartisan legislation-- the *Consumer Mortgage Choice Act* (H.R. 1077) – that would satisfactorily address this important aspect of the ability-to-repay rule. We would urge the subcommittee to support this important legislation.

Thank you for holding this important hearing and for providing us with the opportunity to comment on the ability-to-repay rule on behalf of our member credit unions. If you have any questions or would like further information about any of these issues, please do not hesitate to contact me or NAFCU's Vice President of Legislative Affairs Brad Thaler by telephone at (703) 842-2204 or by e-mail at bthaler@nafcu.org.

Sincerely,

Fred R. Becker Jr.
President & CEO

cc: Members of the Subcommittee on Financial Institutions and Consumer Credit