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Regulations Division  
Office of General Counsel  
Department of Housing and Urban Development  
451 7th Street, S.W.  
Washington, D.C. 20410-0500

Re: Qualified Mortgage Definition for HUD Insured and Guaranteed Single Family Mortgages  
**Docket No. FR 5707-P-01**

Ladies and Gentlemen:

The American Bankers Association<sup>1</sup> appreciates the opportunity to submit comments regarding the Department of Housing and Urban Development's ("HUD") proposed ability-to-repay ("ATR") and qualified mortgage ("QM") loan regulation for single-family mortgage loans that HUD insures or guarantees.

HUD's proposal would implement a Dodd-Frank Act amendment to the Truth in Lending Act ("TILA") that requires residential mortgage lenders to determine an applicant's ability to repay a loan. The Consumer Financial Protection Bureau ("CFPB") has finalized an ability-to-repay regulation that applies to residential mortgage loans across all markets. The Dodd-Frank legislation grants other agencies, including HUD, the authority to define ability-to-repay requirements for loan programs that they administer.

Pursuant to this authority, HUD is proposing rules that define FHA QM thresholds and conditions for FHA loans. HUD's proposal would add to, rather than supplant, existing FHA underwriting and lending standards. In addition, HUD's proposal requires that all FHA loans meet the QM standard, as set forth in the proposed rule.

ABA appreciates HUD's attentive considerations on this important legal reform and respectfully submits the following comments to ensure that the QM provisions are adequately implemented.

## **I. Executive Summary of ABA Comments**

- ABA commends HUD for the proposed rule and for efforts to ensure that the new ability-to-repay/QM triggers do not unduly constrict FHA lending.

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<sup>1</sup> The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's \$14 trillion banking industry and its 2 million employees. Learn more at [www.aba.com](http://www.aba.com).

- The approach taken by HUD’s proposed QM Rule—granting QM status to all single family, forward FHA-insured loans—is commendable and avoids unneeded complications and entanglements with the CFPB’s ATR rulemaking.
- HUD should eliminate any interest rate distinction from FHA’s QM categories, and establish a system where safe harbor treatment is provided to all loans that meet HUD’s proposed QM definition.
- ABA recommends that QM coverage for purposes of HUD insured and guaranteed single family mortgages, must be based on whether the loan qualifies, or is eligible for, FHA insurance or guarantee.
- Industry needs more clarity and understanding about how adjustments to the proposed threshold based on MIP rates will be instituted going forward.
- HUD should create a mechanism by which lenders can cure loans where there was a miscalculation in points and fees or any other failure to satisfy the QM test.
- HUD must consider the burdens associated with the Dodd-Frank mortgage reform regulations, which are set to become effective on January 2014. ABA believes that injecting additional compliance components to these ongoing implementation endeavors is unrealistic given the extensive reforms that are currently pending.

The points set forth above are developed below.

## **II. Triggers & APOR Spreads: HUD should finalize this rule with one single QM definition and one safe harbor legal standard**

ABA believes that the general approach taken by HUD in the proposed QM Rule—granting QM status to all single family, forward FHA-insured loans—is appropriate and avoids unneeded complications and entanglements with the CFPB’s ATR rulemaking. In particular, loans that are insured pursuant to Title I (home improvement loans), Section 184 (Indian housing loans), and Section 184A (Native Hawaiian Housing loans) would, under the proposal, enjoy blanket “safe harbor” QM protection, regardless of the “points and fees” and/or APR levels. ABA commends this straightforward and uncomplicated approach.

Under the proposed rules, a Title II FHA loan would qualify as a “FHA Safe Harbor QM” if the APR does not exceed the APOR for a comparable transaction, as of the date the interest rate is set, by more than the combined annual mortgage insurance premium and 1.15 percentage points. If the APR exceeds the APOR for a comparable transaction by more than the combined annual mortgage insurance premium and 1.15 percentage points, the loan would qualify for rebuttable presumption treatment.

With respect to Title II loans, ABA appreciates HUD’s recognition that the inclusion of the annual mortgage insurance premium (MIP) into the annual percentage rate (APR) calculation will cause many FHA-insured loans to exceed the threshold for safe harbor treatment under the new rules. Informal analysis undertaken by ABA member banks confirms that the addition of such insurance into APR will disqualify a disproportionate number of safe and viable loans from safe harbor treatment. ABA therefore supports HUD’s affirmative attempt in this proposal to ensure that otherwise safe loans are not unnecessarily denied QM safe harbor status.

*Eliminate QM Distinctions:* ABA requests, however, that HUD refrain from finalizing proposals for two different subsets of FHA-insured qualified mortgages. Instead, ABA recommends that HUD eliminate any interest rate threshold from the QM calculation, and establish a system where safe harbor treatment is provided to all loans that meet HUD's proposed QM definition. Under this approach, there would not be two definitions for QM, which means that the APR-APOR spread would be discarded for purposes of FHA QM.

ABA advances this recommendation for two critical reasons—

- Compliance Difficulties: For purposes of the FHA loan program, ABA believes that a safe harbor trigger that is tied to, or varies with, MIP levels is superior to the CFPB's "static" trigger formula. HUD's proposed approach correctly recognizes that changes in insurance costs will inappropriately disqualify safe and sound loans due to the inclusion of the MIP into the triggers. At the same time, ABA notes that instituting a floating threshold will cause considerable compliance hardships and will be difficult to make operational in current lending platforms. In the long run, ABA believes that floating thresholds are likely to become increasingly feasible and easier to manage through automated compliance tools that will be able to automatically and efficiently incorporate MIP price variances into the regulatory thresholds. In the short-run, however, banks believe that such floating triggers will be extremely difficult to implement. ABA is concerned about this short-term impact, and the possible repercussions merit more consideration by HUD.

Banks report that automated compliance tools to handle floating "triggers" do not exist today, and such software will take some time to create. Informal conversations with compliance vendors reveal that industry will need several months to assemble a compliance product that is able to reliably incorporate the proposed floating threshold formula. In the interim, lenders will be required to devise temporary approaches that will require significant alterations to the QM compliance systems that member banks are currently using to implement the CFPB's regulatory amendments. The issues involved in implementing a floating regulatory trigger are very complex, and cannot be done overnight.

We remind HUD that there are six significant new mortgage rules that are scheduled to take effect in January 2014, and the industry is confronted with an unprecedented compliance task. The new rules on the horizon introduce new risk factors and have required complete overhauls of compliance and loan origination systems. Since January of this year, regulators have issued over 4,000 pages of complex final regulations, as well as ongoing rule changes and amendments. These issuances, along with tight timeframes, have worked to create significant operational problems and vendor readiness challenges. Banks across all jurisdictions are expressing serious concerns about having compliant systems by the January 2014 deadline.

In this environment, ABA notes that injecting an additional compliance component to these ongoing implementation endeavors, and doing it this late into the process, is somewhat unrealistic. Banks of all sizes are presently struggling to meet the compliance targets

imposed by the CFPB changes, and many lenders are declaring that lending systems will not meet the deadlines in terms of system testing and compliance assurance. Finalizing an additional rule that imposes a different floating threshold at this time would be unworkable for most banks—particularly small community banks.

- **Unnecessary Distinctions:** ABA believes that, in the FHA context, the distinction between “safe harbor” and “rebuttable presumption” is entirely unnecessary for purposes of advancing consumer protection. FHA standards have evolved over decades, and they closely restrict terms and conditions in a way that assures that each FHA loan has the necessary indicia of repayment ability. FHA guidelines and regulations currently require that all mortgagees perform analysis to determine a borrower’s capacity to repay the mortgage, and require payments that are within the borrower’s reasonable ability to repay.<sup>2</sup> Moreover, as set forth in HUD’s Economic Analysis that accompanies this rule, 93% of loans insured or guaranteed by HUD would qualify for the rule’s safe harbor protections. There is no reason, in this context, to break out a separate rebuttable presumption segment. It appears senseless to impose the significant regulatory burdens and delays associated with a fluctuating threshold for purposes of affecting only 7% of loans insured or guaranteed under Title II.

In conclusion, ABA strongly advises that QM’s safe harbor protections be crafted to apply to the entire QM sector. Once a loan satisfies the QM standards and abides by all FHA guidelines, then it should be protected by a safe harbor, regardless of rate. At a minimum, HUD should treat all QM loans as safe harbor loans, as a temporary measure to ensure that banks are able to properly transition into the new QM regulatory structures. There are many changes occurring at once, and imposing these late and difficult changes on top of ongoing reforms will threaten the integrity of banks’ compliance efforts and threaten banks’ abilities to originate FHA loans. Under our recommendation, lenders would be required to offer and underwrite FHA loans pursuant to the augmented requirements proposed here, but without the added burden of the APOR rate threshold comparison. HUD could still establish a rebuttable presumption category in the future, if it deems necessary to do so.

### **III. Legal Status: HUD should confirm that QM status is conferred based on eligibility for FHA insurance**

The proposed rule generally states that FHA-insured single family mortgages will be deemed to be qualified mortgages (except for HECM mortgages) so long as all program guidelines are observed. In addition, to receive QM protection, FHA-compliant loans must meet the points and fees limitations as implemented by the CFPB final rule.

For purposes of Title I loans, the proposed regulation is rather straightforward—the proposed rule states that “a mortgage insured under Section 2 of title I... is a safe harbor qualified mortgage that meets the ability to repay requirements...” Section 201.7. On the other hand, for Title II loans, the proposal states that “a single family mortgage insured under the National

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<sup>2</sup> See HUD Handbook on *Mortgage Credit Analysis for Mortgage Insurance on One-to-Four Unit Mortgage Loans*. See also 24 CFR §203.33-.47.

Housing Act (that meets the requisite rate and points and fees restrictions) is a safe harbor [or rebuttable presumption] qualified mortgage that meets the ability to repay requirements.” Section 203.19(b)(2) and (b)(3).

ABA is concerned that the broad structure of the proposed legal standard, and how the QM protections apply to specific loan transactions, may pose unintended risk for lenders. As crafted, this proposal raises uncertainty as to what is the precise factor or element that confers QM protection to the creditor making the FHA loan. Under the language employed in proposed Sections 201.7 and .19, it appears that HUD’s proposal would condition QM guarantees upon whether a loan is actually insured by National Housing Act programs. The proposed rule would, therefore, provide that the qualified mortgage status is not based on *eligibility* for insurance, but rather, on *actual* insurance status.

ABA requests that HUD reconsider this approach. ABA recommends that QM coverage for purposes of HUD insured and guaranteed single family mortgages must be based on whether the loan qualifies, or is eligible for, FHA insurance or guarantee. Under this approach, loan or transaction defects that are not related to “ability to repay” would not affect QM coverage. In addition, when there is a subsequent revocation of insurance or guarantee, the loan would retain QM status if it otherwise meets all pertinent underwriting criteria that ensure ability to repay.

ABA requests that HUD consider adding a definitive regulatory statement to this effect, articulating that the safe harbor protections are conferred upon loans that substantively satisfy FHA underwriting standards. The reason for the need for such an explicit statement is that FHA handbooks and guidelines impose a wide variety of requirements that relate not only to underwriting, but also to the mechanics of sale, guarantee, or insurance and post-consummation activities. In light of this, the proposed rule would cause ambiguity if it does not explicitly identify the factor that affords loans with QM protection.

#### **IV. Clarify the Rebuttable Presumption Standard: HUD must provide further clarity on how this standard applies**

Should HUD decide to retain the rebuttable presumption QM category, ABA is concerned that HUD’s proposed legal standard is entirely ambiguous. HUD must provide further clarity on this standard because if banks are unable to determine how this legal standard applies, they may not risk lending in such segments.

As set forth in HUD’s proposal, if a loan is subject to the rebuttable presumption standard, a borrower may rebut the presumption that the creditor met the ability-to-repay standard by proving that the points and fees exceeded the applicable limit or proving that the lender did not make a reasonable and good faith determination of the borrower’s repayment ability. Both prongs of the rebuttable presumption standard raise a number of issues that must be resolved in any final rule.

- *Prong 1--Excessive Points and Fees:* The proposed rule would permit rebuttal of the presumption of compliance by allowing a borrower to show that the loan’s points and fees



are above the 3% cap. We question the utility of this prong. ABA believes this prong has no real value because, under the proposal, FHA loans will not be permitted to have points and fees above the applicable 3% cap. A loan with points and fees above that cap cannot qualify as a QM loan, and under this proposed rule, cannot qualify as a valid FHA loan. It is therefore unclear what the borrower would be challenging under this prong—HUD’s proposed regulation cannot apply to non-FHA loans. Stated differently, it makes little sense to apply a rebuttable presumption standard on loans with fees that exceed the cap because those loans cannot be QM loans.

- *Prong 2--Reasonable and Good Faith Determination of Borrower’s Repayment Ability:* The proposed rule would permit a borrower to rebut the legal presumptions by showing that “the mortgagee did not make a reasonable and good-faith determination of the mortgagor’s repayment ability at the time of consummation, by failing to consider the mortgagor’s income, debt obligations, alimony, child support, monthly payment on any simultaneous loans, and monthly payment (including mortgage-related obligations) on the mortgage, as applicable to the type of mortgage, when underwriting the mortgage in accordance with HUD requirements.”

ABA is concerned with this prong because it appears to articulate elements that are distinct from FHA’s underwriting requirements. We note that, in the judicial/litigation context, differences in term usage will matter greatly—such differences will muddle the burden of proof standard by making uncertain what the parties must present to satisfy their evidentiary burden. For instance, HUD’s proposed rebuttable presumption standard states that borrowers can challenge whether mortgagees considered debt obligations, alimony, and child support. This articulation differs from the corresponding factors that must be analyzed in underwriting as “recurring obligations” other than monthly housing expense as defined in §4155.1 4.C.4.b of the FHA Handbook. The rebuttable presumption standard also refers to “mortgage-related obligations,” a term that is not used in FHA’s Handbook. In addition, the term “monthly payment on simultaneous loans” appears in the proposed rule, but again, FHA’s Handbook does not use this term. There is nothing in the regulations to guide a court about the definition of “monthly payment” or a “simultaneous loan.” These examples, among others, raise much confusion for banks, as institutions cannot predict precise levels of liability. The indefinite standards raise doubt as to whether even full compliance with FHA underwriting requirements would allow a creditor to defend against a rebuttal challenge—a judge faced with differing standards may not be able to recognize which elements must be used, and to what extent.

These examples serve to illustrate the issues that must be clarified as these rules are finalized. HUD should consider that the regulatory standards for rebuttable presumption cannot differ from the underwriting elements that are required for FHA loans. If any differences exist, HUD would be creating new and distinct underwriting standards that vary from FHA underwriting guidelines. In short, distinctions in verbiage between the rebuttable standard and FHA underwriting requirements will result in more than confusion—they will create confusing variations in standards across states and across jurisdictional lines. How any of the factors are calculated for purposes of underwriting and how they are to be considered for

purposes of the QM rebuttable presumption must be tightly aligned or the compliance function will be left in extreme confusion.

Once again, ABA reiterates that HUD can completely avoid these difficult issues. As set forth above, ABA recommends that there be one single playing field in the QM category, and that HUD establish a system where safe harbor treatment is provided to all loans that meet HUD's proposed QM definition. This approach is the most effective way of making FHA lending safe and available to all intended communities.

## **V. Other**

*Process for Adjusting Thresholds:* Industry needs more clarity and understanding about how the adjustments to the proposed threshold based on MIP rates will be instituted going forward. Under HUD's proposal, the thresholds for determining which loans receive the safe harbor protection are expected to fluctuate over time, based on future changes in the MIP levels. In the proposed rule, HUD has not adequately described how such future changes are to be implemented. The industry would need significant notice and lead time in order to implement future changes to this regulatory formula. ABA believes the industry would need, at minimum, four to six months lead notice to ensure proper adjustments to compliance systems regarding threshold level changes.

In defining the process for adjusting the thresholds, ABA requests that HUD issue examples of threshold calculations, and how any start dates would affect any loans that are already in the origination pipeline. Examples should illustrate whether new thresholds apply to loans where an application has already been submitted, and where the adjustment comes between the application and the settlement.

*Cure Provisions:* ABA urges that HUD create a mechanism by which lenders can cure loans where there was a miscalculation in points and fees or any other failure to satisfy the QM test. ABA believes this is particularly important if QM status is to equate with FHA eligibility. These types of procedures encourage early action by lenders and foster more advantageous loans for borrowers. If HUD does not create a mechanism to cure loans where there are QM defects, such loans will simply become uninsurable by FHA in the short run and cause greater caution and lack of credit to consumers over the long term.

*Additional Studies Needed:* Following implementation of a final rule establishing FHA loans as QM safe harbor loans, ABA urges that HUD engage in fuller studies of the marketplace to determine whether— (1) it is necessary to distinguish between FHA safe harbor and FHA rebuttable presumption loans to protect borrowers; and (2) if it is determined that such a dichotomy is necessary, the best means of establishing it. Following such a review, HUD can amend the rule as necessary. In any review, banks respectfully urge that particular attention be given to developing a threshold that is easily applied.

ABA reminds HUD that CFPB has announced that it will be closely monitoring the effects of the ability-to-repay rules on the market and on availability of credit generally. HUD should also

commit to engaging in close supervision of the effects of this law, to ensure that the dual objectives of consumer safety and credit accessibility are consistently met.

### **Conclusion**

ABA appreciates the opportunity to comment on this very important rulemaking. Should you have any questions regarding ABA's comments, please contact the undersigned, or Rod J. Alba, at [ralba@aba.com](mailto:ralba@aba.com).

Sincerely,

A handwritten signature in black ink that reads "Robert R. Davis". The signature is written in a cursive style with a large, stylized "R" at the beginning.

Robert R. Davis