



Bankers Advisory

COMPLIANCE MONITOR

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HUD Releases Qualified Mortgage Definition

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December 11 2013 the U.S. Department of Housing and Urban Development (HUD) released its final rule which defines a 'Qualified Mortgage (QM)' that is insured, guaranteed or administered by HUD. The final rule will be effective on January 10, 2014 and will apply to mortgages with a case number assignment on or after that date.

Final Rule Summary

The *Dodd-Frank Wall Street Reform and Consumer Protection Act* requires HUD to propose a QM definition that is aligned with the *Ability-to-Repay* criteria set out in the *Truth-in-Lending Act (TILA)* as well as the Department's historic mission to promote affordable mortgage financing options for underserved borrowers. HUD's rule builds off of the existing QM rule finalized by the Consumer Financial Protection Bureau (CFPB) earlier this year.

In order to meet HUD's QM definition, mortgage loans must:

- **Require periodic payments without risky features;**
- **Have terms not to exceed 30 years;**
- **Limit upfront points and fees to no more than three percent with adjustments to facilitate smaller loans (except for Title I, Title II Manufactured Housing, Section 184, Section 184A loans and others as detailed below); and**
- **Be insured or guaranteed by FHA or HUD.**

Currently, HUD does not insure, guarantee or administer mortgages with risky features such as loans with excessively long terms (greater than 30 years), interest-only payments, or negative-amortization payments where the principal amount increases. Moreover, HUD's existing underwriting standards require lenders to assess a borrower's ability to repay their mortgage debt. The new limit on upfront points and fees for all Title II non-manufactured housing FHA-insured single family mortgages is consistent with the private sector and conventional mortgages guaranteed by Fannie Mae and Freddie Mac to attain qualified mortgage status under CFPB's final rule.

The rule establishes two types of Qualified Mortgages that have different protective features for consumers and different legal consequences for lenders. HUD's Qualified Mortgage classifies a loan as either Rebuttable Presumption Qualified Mortgages or Safe Harbor Qualified Mortgages depending on the relation of the loan's Annual Percentage Rate (APR) to the Average Prime Offer Rate (APOR), the rate for the average borrow receiving a conventional mortgage. The two categories of Qualified Mortgages are:

1. A Rebuttable Presumption Qualified Mortgage will have an APR greater than APOR + 115 basis points (bps) + on-going Mortgage Insurance Premium (MIP) rate. Legally, lenders that offer these loans are presumed to have determined that the borrower met the Ability-to-Repay standard. Consumers can challenge that presumption, however, by proving that they did not, in fact, have sufficient income to pay the mortgage and their other living expenses.

2. Safe Harbor Qualified Mortgages will be loans with APRs equal to or less than APOR + 115 bps + on-going MIP. These mortgages offer lenders the greatest legal certainty that they are complying with the Ability-to-Repay standard. Consumers can still legally challenge their lender if they believe the loan does not meet the definitions of a Safe Harbor Qualified Mortgage.

Furthermore, HUD's rule covers Title II manufactured housing, Title I manufactured housing and property improvement loans, Section 184 Indian Home Loan Guarantee Program mortgages and Section 184A Native Hawaiian Housing Loan Guarantee Program mortgages. The rule designates loans insured under these programs as *Safe Harbor Qualified Mortgages* regardless of upfront points/fees and APR to APOR ratio so as not to interfere with current lending practices until appropriate parameters can be determined.

HUD also adopts CFPB's list of transactions that are exempt from the ability-to-repay requirements, which includes Reverse Mortgages; Bridge loans with a term of 12 months or less; Construction-to-permanent loans for 12 months or less for the construction phase; Extension of credit by a Housing Finance Agency; Extension of credit by Consumer Development Financial Institutions; Extension of credit made pursuant to a program authorized by sections 101 and 109 of the Emergency Economic Stabilization Act of 2008; Down payment Assistance through Secondary Financing Provider made pursuant to HUD's regulations; Community Housing Development Organization (CHDO) provided that the creditor has entered into a commitment with a participating jurisdiction and is undertaking a project under the HOME program; A 501(c)(3) organization that secured no more than 200 dwellings in the prior calendar year to consumers with income that did not exceed the low- and moderate-income household limit as established pursuant to section 102 of the Housing and Community Development Act of 1974(42 U.S.C. 5302(a)(20)) and the creditor determines, in accordance with written procedures, that the consumer has a reasonable ability to repay the extension of credit.



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