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### REGULATORY REFORM

## Congressional Intent Regarding the Qualified Mortgage Provision



BY RAYMOND NATTER

### Introduction

The Consumer Financial Protection Bureau (CFPB) is currently considering a regulation that could well have a significant impact on the cost and availability of mortgage loans in the United States. The regulation is intended to implement the Qualified Mortgage (QM) provisions in the Dodd-Frank Act (DFA). The DFA imposes significant legal liability on any mortgage originator that does not make a determination before making a mortgage loan that the borrower has a “reasonable ability to repay” the loan. In light of the subjective nature of this standard, the Dodd-Frank Act also establishes a safe harbor from this liability for QM loans, and assigns the CFPB the duty of defining the characteristics of loans that will be considered qualified mortgages. Due to the potential for litigation that arises under the “ability to repay” standard, it is likely that

*Raymond Natter is a partner in the law firm, Barnett Sivon & Natter, P.C. Mr. Natter was the Deputy Chief Counsel at the Office of the Comptroller of the Currency from 1994 until 2005. Mr. Natter represents financial institutions engaged in mortgage lending, but the views expressed in this article are entirely his own.*

few loans will be made that are not QM, and that those that are made will be much more costly.

Currently a debate is raging over whether the Congress intended the definition of a QM loan to be narrow, so that only the very safest loans would be protected, or broad, encompassing the vast majority of non-predatory mortgages. This paper reviews the legislative history leading up to the inclusion of the QM provision in the DFA and concludes that Congress was concerned that a narrow QM might have the unintended consequence of limiting mortgage availability for qualified consumers, and wanted the QM to be inclusive of various types of mortgages, as long as such loans did not have predatory characteristics, or other indicia of highly risky lending.

### Dodd-Frank Act Requirements

#### *The Reasonable Ability to Repay Standard*

Under the Dodd-Frank Act, no creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination, based on documented and verified information, that the consumer has a *reasonable ability to repay the loan*, according to its terms, and all applicable taxes, insurance and assessments.<sup>2</sup> This determination must be made as of the time the loan is consummated.

Failure to comply with the “ability to repay standard” subjects the creditor to civil liability that includes mini-

<sup>2</sup> Public Law 111-203 § 1411 (2010).

mum statutory damages, and potential class action liability. The statutory damages include the consumer's attorney fees. Further, an alleged failure to satisfy the "ability to repay" standard can be raised at any time as a defense to a foreclosure proceeding brought by the holder of the mortgage, whether the holder is the initial lender or an assignee.<sup>3</sup>

#### *Qualified Mortgage Safe Harbor and Rebuttable Presumption*

Section 1412 of the DFA, entitled "Safe Harbor and Rebuttable Presumption," provides that the creditor may *presume* that the loan has met the "ability to repay" standard if the loan is a "qualified mortgage" (QM). The statute lists the minimum qualifications for a QM as:

- There is no negative amortization;
- No balloon payments (except in rural or underserved areas);
- No ability to defer payments of principal, e.g., no "interest only" payments;
- Income and financial resources of the borrower are verified and documented;
- The loan is underwritten based on payments reflecting full amortization and takes into consideration all mortgage-related obligations, such as taxes, property insurance and assessments;
- Variable rate loans are underwritten based on the maximum rate permitted in the first five years and a payment schedule that reflects full amortization;
- Complies with any regulatory guidelines on debt-to-income ratios;
- Total points and fees generally do not exceed 3 percent of total loan amount; and
- The term does not exceed 30 years, unless this limit is extended by regulations;
- In the case of a reverse mortgage, meets guidelines established by regulation.

#### *Significance of QM for Housing Finance*

The QM definition has a very large impact on the availability and cost of housing finance. First, as explained above, a lender making a loan meeting the definition of a qualified mortgage will enjoy at least a presumption of having satisfied the "ability to repay" standard. Anyone making a loan, or purchasing a loan, that is later found to have not met this standard will be subject to significant liability, including the risk that a borrower can raise this issue as a defense to a foreclosure at any time. Thus, even if an originator uses best efforts to comply with the "ability to repay" requirement when making a non-QM loan, the loan will create meaningful liability risks for the originator. Similarly, anyone purchasing a non-QM loan will also face the risk that the borrower can raise the "ability to repay" issue as a defense in any foreclosure action. As a result, both originators and secondary market participants may be very reluctant to make or purchase non-QM mortgages, and

if these mortgages are issued, the cost of the mortgage will increase to reflect this risk.

The definition of QM also is linked to the prohibition on "steering" found in section 1403 of the Dodd-Frank Act. This section prohibits mortgage originators from steering customers to a non-QM loan if the customer could obtain a QM loan. For example, even if a consumer specifically asks for a balloon loan, a mortgage originator cannot offer that product if the borrower would qualify for a QM loan that, by definition, cannot include a balloon payment. In order to avoid potential liability for "steering," it is likely that mortgage originators will only recommend QM loans unless very unusual circumstances exist.

The definition of a QM is also important because under the Dodd-Frank Act, it is directly linked to the imposition of a risk retention requirement. Under section 941 of the Dodd-Frank Act, a "securitizer" or a loan originator has to retain an economic interest in a portion of the credit risk transferred to investors through a mortgage-backed security.<sup>4</sup> This requirement is likely to raise the cost of mortgage lending by making the securitization process more costly and cumbersome for loan originators and securitizers. In light of this concern, the statute exempts securitization transactions for "qualified residential mortgages" (QRM), as such term is to be defined in regulations issued by the federal banking agencies, HUD, FHFA and the SEC.

However, the Dodd-Frank Act states that the definition of a qualified residential mortgage "can be no broader than the definition [of] a qualified mortgage."<sup>5</sup> Therefore, the definition of a QM directly limits the definition of a QRM, and thereby controls the extent to which the banking agencies, HUD, FHFA and the SEC can expand the scope of mortgages that are not subject to risk retention. In other words, a narrowly defined QM eliminates the ability of the other agencies to have a more inclusive definition of QRM, even if these agencies determined that public policy dictates that risk retention should not apply broadly.

Finally, the definition of a QM loan is linked to the ability to include a prepayment penalty in a mortgage loan. Only a QM may include such a penalty, and in any case the penalty must be phased out over a 3-year period.<sup>6</sup>

As a practical matter, faced with the adverse consequences of making a non-QM loan, very few non-QM mortgages will be made. Mortgage originators will face liability for "steering" consumers obtaining non-QM loans, creditors will face liability for failing to comply with the "ability to repay test," and secondary market participants will face the possibility of having to defend against a charge that the loan did not meet the "ability to repay test" for the life of the loan. This alone is likely to make the development of a secondary market for these loans very problematic. This is compounded by the fact that non-QM loans will not qualify for the exemption from risk retention under the QRM test. In light of these impediments, few non-QM loans are likely to be made, and any that are made will be very costly.

<sup>4</sup> The statute permits the risk retention requirement to be allocated between a securitizer and a loan originator. See § 15G(c)(1)(G)(iv) of the Securities Exchange Act of 1934, as added by § 941 of the Dodd-Frank Act.

<sup>5</sup> Dodd-Frank Act § 941.

<sup>6</sup> Dodd-Frank Act § 1414.

<sup>3</sup> Id. at § 1413.

### *Regulatory Discretion to Alter QM Requirements*

The Dodd-Frank Act contains explicit authority for the Federal Reserve Board to revise the qualified mortgage definition.<sup>7</sup> This authority was transferred to the Consumer Financial Protection Bureau (Bureau) on July 21, 2011. The statutory authority to modify the QM definition provides:

The [Bureau] may prescribe regulations that revise, add to, or subtract from the criteria that define a qualified mortgage upon a finding that such regulations are necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of this section, necessary and appropriate to effectuate the purposes of this section and section 129B, to prevent circumvention or evasion thereof, or to facilitate compliance with such sections.<sup>8</sup>

This legislative language is ambiguous. The problem is created by the lack of semicolons in the statutory language that are normally used to separate different alternatives. Without the semicolons, the language is not clear. It can be read as requiring the regulator to make one of four independent findings before issuing regulations,<sup>9</sup> or it can be read as requiring the regulator to make one finding that covers several points.

If this provision is read as providing one of four alternative bases for regulation, the regulator could arguably ignore the impact of its regulations on the availability of responsible and affordable mortgage credit, and base the rule solely on one of the other three factors. This would appear to be an odd result, in light of the concerns that Congress expressed throughout the legislative process that the QM test should not impair the availability of reasonable and affordable mortgages. In fact, as will be discussed in more detail below, the legislative history is quite clear that the phrase concerning mortgage availability was specifically added to the rulemaking provision for the very purpose of ensuring that this factor would be considered by the Bureau in its rulemaking process. Therefore, the better alternative is for the Bureau to consider this factor as a requirement, not as an option.

## Legislative History

### *Prior Legislation*

Attempts to deal with predatory lending in the U.S. Congress can be traced back to legislation first introduced by Representatives Brad Miller and Mel Watt in 2004.<sup>10</sup> However, there was no legislative action on these proposals until the 110<sup>th</sup> Congress, when the

<sup>7</sup> Dodd-Frank Act § 1412. With respect to loans that are issued, guaranteed or administered by the Department of Veterans Affairs, the Department of Agriculture, or the Rural Housing Service, those agencies (in consultation with the Bureau) may establish their own revised standards for the QM.

<sup>8</sup> Dodd-Frank Act § 1412.

<sup>9</sup> This result is obtained by reading the language as if it was drafted as requiring the regulator to make a finding that (i) the regulations are necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of this section; (ii) is necessary and appropriate to effectuate the purposes of this section and section 129B; (iii) to prevent circumvention or evasion thereof, or (iv) to facilitate compliance with such sections.

<sup>10</sup> H.R. 3974, 108<sup>th</sup> Cong. 2<sup>nd</sup> Sess. (2004). See also H.R. 1182, 109<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2005).

House of Representatives passed the Mortgage Reform and Anti-Predatory Lending Act of 2007.<sup>11</sup> As in the Dodd-Frank Act, this bill established an “ability to repay” standard for purchase money mortgages, and included the concepts of a “qualified mortgage” and a “qualified safe harbor mortgage.” The bill authorized the federal banking agencies to prescribe implementing regulations that could “revise, add to, or subtract from the criteria that define a qualified mortgage and qualified safe harbor mortgage . . . to the extent necessary and appropriate to effectuate the purposes of this subsection, to prevent circumvention or evasion of this subsection, or to facilitate compliance with this subsection.”<sup>12</sup> Neither the committee report nor the floor debate relating to H.R. 3915 is helpful in understanding the intent behind this section. However, unlike the Dodd-Frank Act, H.R. 3915 did not include “ensuring that responsible, affordable credit remains available to consumers” as a factor.

In 2009, Representatives Miller and Watt introduced a revised version of H.R. 3915, as H.R. 1728, the Mortgage Reform and Anti-Predatory Lending Act of 2009.<sup>13</sup> This bill eventually was incorporated into the Dodd-Frank Act, and became Title XIV of that legislation.<sup>14</sup>

### *Congressional Hearings*

A hearing on H.R. 1728 was held on April 23, 2009.<sup>15</sup> Concerns were raised that the safe harbor for qualified mortgages was too narrow, and that as a result, the legislation could have the unintended consequence of restricting mortgage credit availability for traditional loans. For example, Representative Capito stated:

While I believe we must take steps to regulate the nontraditional products like interest only or no income verification lending practices, there are a number of traditional lending products in addition to 30-year fixed-rate mortgages that belong in the safe haven (sic) because of their good safety record. I fear that excluding these standard, more traditional products . . . from the safe harbor will serve to place more stress on the housing markets and the overall economy’s ability to recover.<sup>16</sup>

Sandra Braunstein, testifying for the Federal Reserve, stated that the legislation should be modified to afford regulators more rule writing discretion in defining the qualified mortgage. She stated that regulatory flexibility is required in the QM definition in order to allow the regulator to adjust the rules for changes in the mortgage markets and mortgage products.<sup>17</sup> When Representative Castle asked if the safe harbor provision was too narrow, and if regulatory discretion is needed “to guarantee that credit remains available,” Ms. Braunstein agreed.

<sup>11</sup> H.R. 3915 §§ 201 and 203, 110<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2007).

<sup>12</sup> H.R. 3915 § 203 (the subsection referred to has no statement of “purposes.”).

<sup>13</sup> See 156 Cong. Rec. H5235 (June 30, 2010) (Statement of Representative Watt).

<sup>14</sup> *Id.*

<sup>15</sup> Hearings on H.R. 1728, the Mortgage Reform and Anti-Predatory Lending Act of 2009, Before the House Financial Services Committee, 111<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2009).

<sup>16</sup> *Id.* at 4 (emphasis added). See also *Id.* at 22 (Federal Reserve Board witness Sandra Braunstein, noting the adverse implications of making a non-QM loan, stated that such loans would “most likely they would be very high-cost loans.”).

<sup>17</sup> *Id.* at 12-13.

Mr. Castle. The other thing that concerned me that I raised in the opening statement are the safe harbor provisions, which I think are quite narrow, perhaps too narrow. Should there be discretion to adjust the *safe harbors to guarantee that credit remains available to creditworthy perspective home buyers*, and do you have the necessary tools to expand or constrict the safe harbor?

Ms. Braunstein. I think that's right, that there needs to be some discretion on that. We have provided some comments to the committee staff on this issue. There are some loans that would probably be safe prime loans, for instance, right now the way the safe harbor is written, an example is that the term would have to be 30 years. And we know that there are some people in the market who are getting 15-year loans that may be very safe, sound loans. That would not fall into that safe harbor right now, nor would for affordability's sake, some of the loan modifications that are being done, people are being taken to 40-year loans. Those would not be, even though they may be very affordable loans, safe loans. They would not fall into that safe harbor. So, again, I think there is a need to retain some discretion to look at these criteria. And of course we don't know what new products are going to come on the market. So I agree that there probably needs to be some discretion.<sup>18</sup>

Later in the hearing, Ms. Braunstein elaborated further on the need for flexibility in the qualified mortgage definition in order to prevent the impairment of the mortgage markets. Ms. Braunstein stated:<sup>19</sup>

Well, I do think the way the safe harbor is designed that it will drive a lot of the market into that safe harbor. . .

. . . But there are some things that it's important not to define such that you are eliminating the ability to get loans that otherwise would be safe and sound, and good loans for consumers, which is why we have recommended that there be some flexibility given to the rule writers in terms of being able to make adjustments to that safe harbor.

And in particular that is going to be important when the mortgage markets reemerge and redevelop themselves. We don't know what kinds of products will be developed in the future and we may need to adjust it either way. It's not just loosening it, but there may be things that aren't contained now that would need to be added to it to protect consumers.

Other witnesses also voiced concerns that a narrowly drawn safe harbor could inappropriately constrict mortgage credit availability. For example, the Conference of State Banking Supervisors noted that the safe harbor in the bill might be too strict and could have an impact on credit availability, and urged that it has to be "very carefully drafted" to avoid that result.<sup>20</sup> The National Association of Realtors testified that due to the other provisions in the bill, lenders will not offer products outside of the safe harbor, and the safe harbor needs to be expanded to prevent an adverse impact on mortgage credit availability.<sup>21</sup> The Mortgage Bankers Association testified that the definition of a qualified mortgage is far too limited and as a result, the bill would raise costs on

a broad variety of safe mortgage products.<sup>22</sup> This association recommended that the regulators should be given the authority to include loans in the QM definition unless they contain specific higher risk factors, such as negative amortization. The Independent Community Bankers of America gave similar testimony, noting that without a wider safe harbor, the legislation could cause rigidity that prevents lenders from serving local markets.<sup>23</sup>

Based on the hearing record, it is clear that there were significant concerns about the adverse consequences of a narrow definition of a "qualified mortgage" on the mortgage availability for qualified borrowers. The Federal Reserve Board (which at the time of the hearing was designated as the implementing agency) believed that further regulatory flexibility was necessary in designing the safe harbor in order to ensure that safe loans would continue to be made to meet the needs of creditworthy borrowers, and to restore the private mortgage markets. The Federal Reserve noted that additional flexibility would allow the regulator to both expand the QM to include safe loans, and to address new types of unsafe loans that may develop in the future. There was no indication in the hearing that the QM should exclude safe loans in order to establish a market for non-QM mortgages.

#### Committee Mark Up

The House Financial Services Committee proceeded to mark up the bill on April 28, 2009.<sup>24</sup> During the Committee's consideration of the measure, Representative Moore offered an amendment that made one of the purposes of the legislation "ensuring that responsible, affordable mortgage credit remains available to consumers."<sup>25</sup> Congressman Moore explained that the amendment is intended to address his concern that the bill could prevent responsible borrowers from having access to mortgage credit.<sup>26</sup> Congressman Hensarling noted that the Moore amendment is important because the "purposes" of the legislation must be considered by the regulator when issuing regulations to define the safe harbor, and that the amendment would ensure that the legislation does not deprive creditworthy consumers out of homeownership opportunities.<sup>27</sup> Congressman Watt stated that he was supportive of the concept, but wanted the language placed elsewhere in the bill.<sup>28</sup> Congressman Watt referred to the fact that a later amendment would be included in the bill to expand the definition of a qualified loan (the Bean-Castle Amendment<sup>29</sup>) and, therefore, was uncertain how the Moore amendment would interact with the Bean-Castle

<sup>22</sup> *Id.* at 64.

<sup>23</sup> *Id.* at 66.

<sup>24</sup> The video recording of the mark up may be found at: <http://archives.financialservices.house.gov/Hearings/hearingDetails.aspx?NewsID=803>.

<sup>25</sup> Moore Amendment No. 14.

<sup>26</sup> Mark up video at the 1:45 – 1:50 time marks.

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> The Bean-Castle Amendment deleted provisions in the bill limiting the QM to 30-year, fixed rate products. In addition, the amendment included as a QM mortgages issued, guaranteed or administered by certain federal agencies and loans that meet the underwriting standards used by Fannie Mae or Freddie Mac. Representative Bean explained that the amendment "balances our efforts to rein in the excesses of the subprime market with the need to preserve access to credit for respon-

<sup>18</sup> *Id.* at 13-14 (emphasis added).

<sup>19</sup> *Id.* at 27.

<sup>20</sup> *Id.* at 18-19, 35.

<sup>21</sup> *Id.* at 70, 83, 84.

amendment. Chairman Frank disagreed with Mr. Watt, explaining that “it was the regulators who asked us to do this.” The Chairman stated that he would work with Watt and Moore to make sure that the amendment links up correctly with the safe harbor, presumably in light of the Bean-Castle amendment.<sup>30</sup> The Moore amendment passed by a voice vote of the Committee.

Later in the mark-up, following passage of the Bean-Castle amendment, Chairman Frank asked that the prior vote on the Moore amendment be rescinded, and that a new version of the amendment be considered.<sup>31</sup> Representative Moore then offered a revised version of his amendment that moved the key language from the purposes section of the bill to the “findings” section.<sup>32</sup> Representative Moore argued that the change would have no substantive effect.<sup>33</sup> But Congressman Hensarling disagreed, noting that the safe harbor provision refers the regulator to the “purposes” section, and, therefore, moving the language to the “findings” section would not require the regulator to consider the impact of the mortgage markets when issuing regulations. Mr. Hensarling stated that it was important that the bill ensure that the regulator consider the overall mortgage markets are not damaged. Chairman Frank acknowledged that Mr. Hensarling had valid concerns, and responded to his objection:

That is a fair point. . . I will *guarantee* that by the time this bill reaches the floor it will be clear that it will have the same substantive impact [as the original amendment]. . . We have no intention of weakening the mortgages. Yes, it is a problem when people get mortgages they shouldn't get. It has been a historically greater problem that some people couldn't get mortgages they *should* get. I will *guarantee* to the gentleman [Representative Hensarling] that doesn't happen.<sup>34</sup>

In sum, Congressman Moore offered an amendment to ensure that regulatory changes to the QM definition would not have an adverse impact on availability of responsible and affordable mortgage credit. During the process of adopting this amendment, the operative language was moved from the “purposes” section to the “findings” section, which would have lessened the impact of the amendment on regulatory decision-making. When this was pointed out to Chairman Frank, he *guaranteed* that it would be fixed on the floor, and expressed strong support for ensuring that the regulations issued in connection with the QM do not have the effect of preventing people from getting mortgages that should get them.

The statements of Chairman Frank could not be clearer: he did not intend the QM to interfere with the ability of creditworthy borrowers from obtaining mortgage products. Further, the Bean-Castle amendment

was not sufficient to allay the Chairman's concerns. He insisted on including the Moore amendment in order to make sure that the regulator would consider mortgage availability when implementing the QM, and when the Chairman realized that the language passed in the Committee might not be sufficient, the Chairman guaranteed that it would be corrected on the floor.

#### *Floor Consideration*

As noted, during the Committee mark up, Chairman Frank promised that the bill language would be changed to make sure that the intent of the Moore amendment would be carried out. Mr. Frank carried out this promise.

During House floor consideration, Chairman Frank introduced a manager's amendment that made two changes relevant to this issue.<sup>35</sup> The first change was to section 105 of the bill. As introduced, this section directed the federal banking agencies to issue joint regulations to prohibit terms, acts or practices relating to residential mortgages that the agencies find to be abusive, unfair, deceptive, predatory, or necessary or proper to effectuate the purposes of the legislation. The Frank amendment modified this section to add that the regulations are to be “necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of this section and [the “ability to repay” requirement].”<sup>36</sup>

The second provision in the manager's amendment modified the regulatory authority to change the QM standard. The Frank amendment provides that the regulator may promulgate regulations to revise, add to or subtract from the criteria for a QM mortgage upon a finding that such regulations are “necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of this section.”<sup>37</sup>

Thus, under the Frank manager's amendment, both the general rulemaking authority to prohibit unfair, deceptive or predatory practices, and the specific rulemaking authority to modify the QM definition, contain an explicit reference to a finding that regulations are “necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers” in a manner consistent with the purposes of the legislation.

Chairman Frank did not elaborate on these two provisions in the manager's amendment during the floor debate. However, in arguing against an amendment offered by Representative Price requiring the Federal Reserve to certify that the legislation would not increase the price or reduce the availability of qualified mort-

*sible borrowers and those working with stable, successful government programs* that are designed to boost homeownership.” See, <http://www.votesmart.org/public-statement/422794/bean-hails-mortgage-reform-passage>.

<sup>30</sup> *Id.* Mr. Frank's statement that he would work to make sure the amendment links up correctly with the safe harbor was in response to Representative Watt's concern about the relationship of the Moore amendment and the Bean-Castle amendment. Therefore, Mr. Frank's comment must refer to linking up the Moore language with the Bean-Castle language.

<sup>31</sup> *Id.* at the 4:55—4:59 time mark.

<sup>32</sup> Moore amendment No. 23.

<sup>33</sup> Video at 4:55—4:59 time marks.

<sup>34</sup> Video at 4:55—4:59 time marks. Emphasis added.

<sup>35</sup> Frank amendment No. 1, 155 Cong. Rec. H5343 (May 7, 2009).

<sup>36</sup> *Id.* The language appears at § 1405 of the DFA: “The Board shall, by regulations, prohibit or condition terms, acts or practices relating to residential mortgage loans that the Board finds to be abusive, unfair, deceptive predatory, necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of this section and section 129C, necessary or proper to effectuate the purposes of this section and section 129C, to prevent circumvention or evasion thereof, or to facilitate compliance with such sections, or are not in the interest of the borrower.”

<sup>37</sup> *Id.*

gages, Chairman Frank stated that the purpose of the bill was not to increase the availability of credit, but instead to strike a balance between preventing lenders from making loans to consumers who are not able to repay the loan and credit availability. Chairman Frank explained that he thought the bill achieved that balance:

Let's understand the problem. Too many loans were made to people who shouldn't have gotten them. . . . (O)ne of the important purposes of this bill is to reduce the pattern of people getting loans who shouldn't have gotten them because they couldn't repay them. . . . Now you want to do it with balance and you want to do it in a reasonable way. I believe we deal with that.<sup>38</sup>

During debate on another amendment, Representative Watt likewise referred to the "delicate balance" that was made in crafting the bill to "protecting consumers and protecting the availability of funds."<sup>39</sup>

These statements are consistent with the view that the definition of a qualified mortgage is intended to strike a balance, and that it is not intended to be so narrow as to interfere with the provision of mortgages to creditworthy borrowers.

The House approved H.R. 1728, the Mortgage Reform and Anti-Predatory Lending Act of 2009, on May 7, 2009, by a vote of 300-114.<sup>40</sup>

#### *Incorporation into the Dodd-Frank Act*

The text of the Mortgage Reform and Anti-Predatory Lending Act, as passed by the House, was added to H.R. 4173, the bill that became the Dodd-Frank Act, during floor consideration of that measure.<sup>41</sup> A floor amendment was adopted that specified that a qualified mortgage includes reverse mortgages that were either insured by FHA or met the APR limitations applicable to qualified mortgages.<sup>42</sup> There was no discussion on the House floor on these provisions.

In the Senate, an ability to repay provision was added to S. 3217, the Senate precursor to the Dodd-Frank Act, through a floor amendment offered by Senators Merkley, Klobuchar, Schumer, Snowe, Brown (MA), Begich, Boxer, Dodd, Kerry, Franken and Levin.<sup>43</sup> The amendment established a presumption that the "ability to repay" test is met if the creditor took specific steps when underwriting the loan, such as verifying income and assets, and using the fully phased in interest rate to qualify borrowers. The "specific steps" were very similar to the qualified mortgage definition in the House bill.

The conference report adopted the House language creating a category of loans as being "qualified mortgages," and authorizing the regulator to:

"(P)rescribe regulations that revise, add to, or subtract from the criteria that define a qualified mortgage upon a finding that such regulations are necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes of this section, necessary and

appropriate to effectuate the purposes of this section and section 129B, to prevent circumvention or evasion thereof, or to facilitate compliance with such sections.<sup>44</sup>

#### *Statutory Language Changes in the Scope of the Qualified Mortgages*

A review of the statutory language used in the bills leading up to the qualified mortgage provisions in the Dodd-Frank Act also evidences a Congressional intent for a broad, and not a narrow, qualified mortgage definition. During the legislative process, Congress increased the scope of the QM basket, making the test definition more and more inclusive. For example, the limitation on permissible points and fees was raised from 2 percent to 3 percent, a higher point and fee cap was authorized for smaller loans, interest rate caps were deleted, the standard for underwriting variable rate loans was made more flexible, and the requirement that the QM had to be a 30 year mortgage was modified to permit shorter term loans, and with regulatory authorization, loans in excess of 30 years. These, and other bill language changes demonstrate a Congressional interest in broadening the QM in order to accommodate all responsible lending products, and with Congressional concern that non-QM loans would not be readily available at a reasonable cost. Thus, these modifications strongly support the position that the Congress did not intend, and the Bureau should not implement, a narrow qualified mortgage definition in order to foster a market for non-QM loans.

## **Conclusion**

Title XIV of the Dodd-Frank Act establishes substantive mortgage lending standards upon mortgage creditors, including a requirement not to make a loan to a consumer unless the creditor makes a reasonable and good faith determination that the consumer has a reasonable ability to repay the loan according to its terms. Failure to meet this requirement can result in significant civil liability for the creditor. In addition, such failure can be raised as a defense to a foreclosure action at any time, and this defense can be raised against subsequent purchasers of the mortgage loan.

In order to avoid some of the adverse consequences that would result if any loan could be challenged based on an alleged violation of this standard, the bill also creates a presumption that a creditor that makes a loan that meets the definition of a "qualified mortgage" or QM has complied with the "ability to repay" standard. The statute contains a list of criteria that are to be used for defining a QM, but then includes authority for the regulator to adjust the criteria through regulations. Such adjustments may revise, add to or subtract from the statutory factors.

While the legislative language is not totally clear, the legislative history indicates that Congress was still concerned that the QM test could inadvertently limit credit availability to creditworthy borrowers, even after it was amended to include more types of mortgages (Bean-Castle amendment). Chairman Frank was so concerned about the possibility of unduly constricting credit, that he *guaranteed* that the issue would be addressed in the

<sup>38</sup> 155 Cong. Rec. H5358 (May 7, 2009).

<sup>39</sup> 155 Cong. Rec. H5355 (May 7, 2009).

<sup>40</sup> 155 Cong. Rec. H5370 (May 7, 2009).

<sup>41</sup> 155 Cong. Rec. H14408-9 (Dec. 9, 2009). According to House Resolution 956, the text of H.R. 1728 was added automatically upon consideration of H.R. 4173. This is known as a "self executing" amendment.

<sup>42</sup> 155 Cong. Rec. H14663 (Dec. 10, 2009).

<sup>43</sup> SA 3962 to S. 3217; 156 Cong. Rec. S3558-3559 (May 11, 2010).

<sup>44</sup> H. Rep. No. 111-517 (Conf.) 111th Cong. 2d Sess. (2010). In light of the fact that the Conference adopted the House version of this provision, the legislative history of the House bill is most relevant in determining congressional intent.

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final legislation. Chairman Frank followed through, and amended the bill on the House floor to include a reference in two different rule writing sections that notes the need to “ensure that responsible, affordable mortgage credit remains available to consumers in a manner consistent with the purposes” of the ability to repay requirement.

There is nothing in the legislative history or statutory language to indicate that the QM was intended to be a narrow standard, or that Congress wanted to establish a vibrant market to develop for non-QM loans. The legislative history shows that the opposite is the case. Even

after the adoption of the Bean-Castle amendment, Congress was concerned the QM standard might be too narrow, and expected the regulator to use its rulemaking authority to modify the QM to ensure that mortgage credit remains available to creditworthy consumers. The legislative history demonstrates an effort to include as many “safe” loans as possible within the QM umbrella, and to exclude only those loans that create predatory type risks to consumers. The Bureau should carefully consider this legislative history when issuing regulations regarding the scope of the QM.