Section 35 (ATR/QM) Breakdown

General:

This section applies to any consumer credit transaction that is secured by a dwelling, as defined in § 1026.2(a)(19), including any real property attached to a dwelling.

Therefore, any loan that is not primarily for a consumer purpose (such as primarily for a business, commercial, or agricultural purpose) is not covered by this requirement, even if secured by a dwelling. A loan for investment property must be analyzed to determine if it is primarily for consumer or commercial purpose, in accordance with 1026.3 and associated commentary.

Similarly, this section does not apply to any modification/change to an existing loan that is not treated as a refinancing under 1026.20(a).

Any loan not secured by a dwelling (such as vacant land) is also not subject to this requirement.

Per 1026.2(a)(19) "***Dwelling***" means a residential structure that contains one to four units, whether or not that structure is attached to real property. The term includes an individual condominium unit, cooperative unit, mobile home, and trailer, if it is used as a residence. Therefore, Section 43 covers: Purchase and Refinance transactions on first and second liens for:

- Principal residence;
- Secondary residence; **or**
- Vacation residence

Exemption Types for all of Section 43:

- Mortgage transactions secured by a Timeshare; or
- Home Equity Line of Credit subject to §1026.40 (open-end). Important note:
  - ➢ Only HELOCs secured by the *consumer's (borrower's)* dwelling (as defined above) are exempt. If the HELOC is secured by a dwelling pledged by a non-borrowing grantor, then it is a covered transaction subject to Section 43 requirements.
  - ➢ 1026.43 warns creditors not to structure a consumer's dwelling loan as a HELOC to evade Ability To Repay underwriting requirements. If a creditor documents a loan as open-end credit but the features and terms, or other circumstances, demonstrate that the loan does not meet the definition of open-end credit, the loan is subject to all rules for closed-end credit, including Section 43.

Exemption Types for ATR and QM classifications *:

- Reverse mortgages subject to § 1026.33
- Temporary or "bridge" loans with a term of 12 months or fewer;
- A construction phase of 12 months or less on a construction-to-permanent loan (longer than 12 months is not exempt); or
- Loans made in connection with a program by HFA, DFIs, DA, or other specific Non-profits.

* Note: This exemption does NOT include prepayment penalty provisions. These loans are strictly limited in their ability to charge a prepayment penalty per 1026.43(g)

The Qualified Mortgage (QM) Effective March 1, 2021

Qualified Mortgages are broken down into five main classifications:

1. **QM General (available to creditors of all sizes)**: §1026.43(e)(2)
    - Meets all QM requirements and Underwritten as per specific guidelines in §1026.43(e)(2).
    - Must qualify based on a fully amortizing schedule using the max rate permitted during the first 5 years after the 1st regular payment due date
    - Contains no "toxic" loan features such as balloon payments, terms in excess of 30 years, interest only payments, or negative amortization;
    - Must pass Points and Fees test (as set forth in §1026.32(b)(1)); and
    - Must pass APR test found under §1026.43(e)(2)(vi).
        - ➢ For a first-lien covered transaction with a loan amount greater than or equal to $134,841, the APR exceeds APOR for a comparable transaction by less than 2.25 percentage points;
        - ➢ For a first-lien covered transaction with a loan amount greater than or equal to $80,905 but less than $134,841, the APR exceeds APOR for a comparable transaction by less than 3.5 percentage points;
        - ➢ For a first-lien covered transaction with a loan amount less than $80,905, the APR exceeds APOR for a comparable transaction by less than 6.5 percentage points;
        - ➢ For a covered transaction secured by a manufactured home with a loan amount less than $80,905, the APR exceeds APOR for a comparable transaction by less than 6.5 percentage points;
        - ➢ For a covered transaction secured by a manufactured home with a loan amount equal to or greater than $134,841, the APR exceeds APOR for a comparable transaction by less than 2.25 percentage points;
        - ➢ For a subordinate-lien covered transaction with a loan amount greater than or equal to $80,905, the APR exceeds APOR for a comparable transaction by less than 3.5 percentage points; and
        - ➢ For a subordinate-lien covered transaction with a loan amount

less than $80,905, the APR exceeds APOR for a comparable transaction by less than 6.5 percentage points.

2. **QM Agency**: §1026.43(e)(4) Defined as QM by the US Dept. of HUD, US Dept. of VA, or US Dept. of Agriculture.
    - The Agency QM rules retain the current product feature limitations.
    - For FHA loans, the standard points and fees test will apply. An FHA loan will have a rebuttable presumption if the APR exceeds the APOR by more than 2.00%.
    - For VA loans, there is no points or fees test. There is also no APR/APOR test for rebuttable presumption.
    - For USDA loans, the interest rate must be fixed, and the standard points and fees test will apply. There is also no APR/APOR test for rebuttable presumption.

3. **QM Balloon:** §1026.43(f)
    - Classification provided for creditors who pass the “Rural and Underserved” test set forth by the CFPB.
        - ➢ Creditor has extended a single covered transaction in a “Rural or Underserved” area during the previous calendar year; or, during either of the two preceding calendar years, if the application is received prior to April 1st;
        - ➢ Creditor and affiliates have fewer than 2000 first lien covered transactions during the previous calendar year, not including those held in portfolio by creditor or affiliate; and
        - ➢ Together with its affiliates, has less than $2.167 billion (2019) in assets during the previous calendar year (adjusted annually per CPI).
        - ➢ Grace period through April 1st of following year to comply.
    - Meets certain QM requirements including:
        - ➢ Payments do not result in an increase of the principal balance;
        - ➢ Term does not exceed 30 years;
        - ➢ Points and Fees limitation
        - ➢ No toxic features, except balloon
    - Exempt from Balloon exclusion.
    - HPCT threshold increased to 3.5% to allow these loans to maintain safe harbor status.
    - Required to be held in portfolio for at least 3 years, and cannot be subject to a forward commitment or loses QM status; with exception of transfer to qualified “Small Creditor”
    - Permanent exception to Section 32 balloon restriction (1026.32(d)(ii)(c)
    - Balloon loans under this classification are restricted by;
        - ➢ Calculating payments based on a maximum 30-year

amortization

- ➢ Interest rate cannot increase over the term (fixed rate); and
- ➢ Minimum loan term of 5 or more years.

4. **QM Small Creditor:** §1026.43(e)(5)

- Classification to allow small creditors to continue to operate with specific beneficial exemptions.
- Creditor and affiliates have fewer than 2000 first lien covered transactions during the previous calendar year, not including those held in portfolio by creditor or affiliate; and
- Together with its affiliates, has less than $2.167 billion (2019) in assets during the previous calendar year (adjusted annually per CPI).
- Grace period through April 1st of following year to comply.
- HPCT threshold increased to 3.5%, allowing them to maintain safe harbor
- No restriction on geographic location
- Must pass Points and Fees test (as set forth in §1026.32(b)(1))
- No negative amortization, interest only, or balloon features.
- Required to be held in portfolio for at least 3 years and cannot be subject to a forward commitment or loses QM status; with exception of transfer to another designated "Small Creditor".
- Must establish reasonable ability-to-repay.
  - ➢ Must qualify based on a fully amortizing schedule using the max rate permitted during the first 5 years after the 1st regular payment due date

5. **QM Seasoned Loan**

- Fixed-rate;
- No negative amortization; and
- Meets performance and portfolio requirements in § 1026.43(e)(7)(ii) & (iii).
  - ➢ The loan is secured by a first lien.
  - ➢ The loan has a fixed rate.
  - ➢ The loan has regular, substantially equal periodic payments that are fully amortizing, does not allow negative amortization, and does not have a balloon payment. A loan has fully amortizing payments if periodic payments of principal and interest will fully repay the loan over the loan term.
  - ➢ The loan term does not exceed 30 years.
  - ➢ The loan is not a high-cost mortgage as defined in Regulation Z, 12 CFR 1026.32(a).
  - ➢ The total points and fees cannot exceed 3 percent of the loan amount.
  - ➢ There cannot be an investor.

- Loans must meet underwriting and verification requirements and meet certain performance requirements at the end of the 36-month seasoning period.

Overall QM requirements:

No Toxic Features:

- Balloon (except as indicated above in QM Balloon category; or
- Interest-only; or
- Negative Amortization; or
- Term exceeding 30 years

Prepayment Penalties:

- Permitted only on *Non-HPCT QM (see page 7 for further explanation);
- Fixed or Step Rate only;
- Cannot exceed 3 years following consummation; and
- Must not exceed 2% if incurred during the first 2 years; and 1% if incurred during the third year.

Points and Fees

A covered transaction is not a Qualified Mortgage unless the transaction's total points and fees, as defined in § 1026.32(b)(1), do not exceed: (all amounts to be indexed annually for inflation) (2021)

- For a loan amount greater than or equal to $134,841: 3% of the total loan amount;
- For a loan amount greater than or equal to $80,905 but less than $134,841: $4,045;
- For a loan amount greater than or equal to $26,968 but less than $80,905: 5% of the total loan amount;
- For a loan amount greater than or equal to $16,855 but less than $26,968: $1,348;
- For a loan amount less than $16,855: 8% of the total loan amount.

Points and Fees include(§ 1026.32(b)(1)):

- All items required to be disclosed in “finance charges” §1026.4(a-b):
  - Except for interest or time-price differential; and
  - Any amount in excess of FHA UFMIP, for Federal or State agency guaranty or mortgage insurance; Non-Agency MI payable after consummation; or

for

➢ Non-Agency MI payable at or prior to closing, unless refundable on a pro- rata basis;

- Less excludable discount points; **(See Bona Fide Discount section below)
- All compensation or fees paid directly or indirectly to creditor, loan originator or its affiliates known at consummation;
- All items listed as real-estate related fees, unless reasonable, and creditor or affiliate receives no direct or indirect compensation for charge;
- Premiums for any credit insurance payable at or before consummation;
- Maximum Prepayment Penalty that may be collected if allowable;
- Total Prepayment penalty incurred if the borrower refinances with creditor or its affiliate; and
- Any compensation paid by creditor to a mortgage broker.

*ATR Presumptions of Compliance for QMs

- **QM- Non-HPCT** (Prime Loans) = **Safe Harbor** and presumption of compliance with ATR requirements. Lower risk for delay or issue upon occurrence of default.
- **QM-HPCT** (Sub Prime Loans) = **Rebuttable Presumption** of compliance with all ATR requirements. Borrower has ability to rebut the creditor's compliance with requirements for a minimum of 3 years. Creditor must prove its compliance with ATR by valid documentation which can lead to delays, fines, and additional liabilities upon occurrence of default.
- **QM-Seasoned Loan = Safe Harbor and presumption of compliance with ATR requirements regardless if HPCT or not.**
- **Non-QM** = No presumption of compliance with ATR requirements.

****Bona Fide Discount Points:** An amount equal to each 1 point charged that reduces the interest rate over the term of the loan, by an industry standard amount (generally 1/8th % (.125)).

- Up to 2 bona fide discount points can be excluded if pre-discounted rate does not exceed APOR by more than 1%.
- Up to 1 bona fide discount points can be excluded if pre-discounted rate does not exceed APOR by more than 2%.

What is the benefit of doing a QM? While the ATR standard is required by regulation, achieving QM status is optional. A creditor gains the following benefits by going the extra mile to obtain a QM:

- Presumption of Compliance
- If the loan is a Higher Priced Mortgage Loan, relief from the more stringent appraisal requirements of 1026.35(c)

The Legacy Qualified Mortgages – Sunset October 1, 2022

1. QM General (available to creditors of all sizes):§1026.43(e)(2)

- Meets all QM requirements and Underwritten as per specific guidelines in Appendix Q, with use of 8 ATR determining factors.
- Must qualify based on a fully amortizing schedule using the max rate permitted during the first 5 years after the 1st regular payment due date (this is more stringent than plain ATR requirements which do not require the payment be computed at the max rate in 5 years, unless it is a balloon).
- Contains no "toxic" loan features such as balloon payments, terms in excess of 30 years, interest only payments, or negative amortization;
- Must pass Points and Fees test (as set forth in §1026.43(e)(3)); and
- Maximum debt-to-income ratio of≤43%.

2. QM Agency/GSE Eligible: §1026.43(e)(4) (The GSEs have announced that they will no longer purchase loan that do not meet the new revised General QM standard for loan with application dates after July 1, 2021)

- Meets government-sponsored enterprise (GSE), government guaranteed or insured underwriting and salability requirements. Examples: Fannie Mae (FNMA), Freddie Mac (FHLMC), FHA, VA and USDA;
- The loan must receive the approval from the GSE automated underwriting service (Ex: DU or LP), and meet conditions provided therein, but is not required to be sold to the GSE in order to receive this classification;
- Contains no "toxic" loan features such as balloon payments, terms in excess of 30 years, interest only payments, or negative amortization;
- Must pass Points and Fees test (as set forth in §1026.43(e)(3)); and
- Not limited to Appendix Q underwriting guidelines.