

FAQs On ATR & QM Rules For Small Entities – Part One

By

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Introduction. *The FAQs below come directly from the most recent CFPB guidelines for January 2014. As I go through the rules I will supplement the FAQs. This information does not apply to the Big Banks, e.g. B of A, Morgan Stanley, JPMorgan, etc. Rather, it applies to “small creditors” such as community banks. Unfortunately, the regulators have sought to apply the ATR/QM rules even to Mom and Pop who may sell an occasional rental unit or two.¹ The CFPB gives “small creditors” or “small entities” certain underwriting latitude in the application of the ATR/QM rules. Generally, these are persons or entities with no more than \$2 billion in assets that make no more than 500 mortgage loans per year. Originally, the small entity exceptions were intended to apply only to “rural or underserved counties,” but until January 10, 2016, the exceptions will apply to all small creditors, regardless of location. Caveat: This material below is informational only and does not constitute “legal advice.” Moreover, it is summary only, and for more information, the actual regulations should be reviewed.*

1) What are the ATR/QM rules all about? *They require that you make a reasonable, good-faith determination before or when you consummate a mortgage loan that the consumer has a reasonable ability to repay the loan, considering such factors as the consumer’s income or assets and employment status (if relied on) against:*

- *The mortgage loan payment;*
- *Ongoing expenses related to the mortgage loan or the property that secures it, such as property taxes and insurance you require the consumer to buy;*
- *Payments on simultaneous loans that are secured by the same property;*
- *Other debt obligations, alimony, and child-support payments.*

2) When do I have to start following these rules? *The rule applies to covered transactions for which you receive an application on or after January 10, 2014.*

3) What transactions are covered? *Almost all closed-end consumer credit transactions secured by a dwelling including any real property attached to the dwelling. This means loans made to consumers and secured by residential structures that contain one to four units, including condominiums and co-ops. NOTE: The ATR/QM rule is not limited to first liens or to loans on primary residences.*

4) What transactions are excluded? *The ATR and QM rules do not apply to:*

- *Open-end credit plans (home equity lines of credit, or HELOCs);*
- *Time-share plans;*
- *Reverse mortgages;*

¹ I maintain vehemently that on the state and federal levels, the CFPB rules do *not* apply to the occasional sale of residential property owned by persons who are not in the business of making such loans, when they “carry back the paper,” e.g. on a contract or note and trust deed. The fact that Oregon’s DFCS insists otherwise is a sad and disturbing commentary on the uber-regulatory mindset of governmental bureaucrats who would rather regulate than cogitate. Any sentient human being who has a passing familiarity with the housing and credit crisis would know that the occasional sale of residential property by Mom and Pop who carry back the paper, was never meant to be subject to the ATR/QM and mortgage loan originator laws.

- Temporary or bridge loans with terms of 12 months or less (with possible renewal);
- A construction phase of 12 months or less (with possible renewal) of a construction-to-permanent loan;
- Consumer credit transactions secured by vacant land;
- In addition, certain types of creditors or loan programs may be exempt from the ATR requirements.

5) How long do I have to keep records on compliance with the rules? *Three years after consummation of the transaction – although you may want to keep records longer for business purposes.*

6) Specifically, what is ATR and what standard does it set? *The term “ATR” stands for “ability to repay.” Under the general ATR standard, you must make a reasonable, good-faith determination that the consumer has a reasonable ability to repay the loan before (or when) you consummate a covered mortgage loan transaction.*

7) What factors must I consider in making that determination? *There are eight factors you must consider in your underwriting of the loan [Note: The rule does not preclude you from considering additional factors, but you must consider at least these eight factors]:*

- Current or reasonably expected income or assets [excluding the value of the property that secures the loan] that the consumer will rely on to repay the loan;
- Current employment status [assuming you rely on employment income when assessing the consumer’s ability to repay];
- Monthly mortgage payment for this loan. [This is calculated by using the introductory or fully-indexed rate, whichever is higher, and monthly, fully-amortizing payments that are substantially equal.];
- Monthly payment on any simultaneous loans secured by the same property;
- Monthly payments for property taxes and insurance that you require the consumer to buy, and certain other costs related to the property such as homeowners association fees or ground rent;
- Debts, alimony, and child- support obligations;
- Monthly debt-to-income ratio or residual income, that you calculated using the total of all of the mortgage and non-mortgage obligations listed above, as a ratio of gross monthly income;
- Credit history.

8) What type of credit history should I be looking for? *Here’s what the CFPB says:*

- A credit report generally is considered a reasonably reliable third-party record for verification purposes.
- While the rule requires that you examine credit history, it does not prescribe a particular type of credit history to consider or prescribe specifically how you should judge the information you receive. Your consideration of credit history must be reasonable in light of the facts and circumstances.
- Credit history might include information about:
 - Number and age of credit lines;
 - Payment history;
 - Judgments;
 - Collections;
 - Bankruptcies;

- *Nontraditional credit references such as rental payment history or utility payments [If you know, or have a reason to know, that the information on a consumer's credit report is inaccurate, you can ignore it. For example, there might be a fraud alert or a dispute on the credit report, or the consumer may present other evidence that contradicts the credit report. In those cases, you may choose to disregard the inaccurate or disputed items.];*
- *If the consumer lists a debt obligation that does not show up on the credit report, you may accept the consumer's statement about the existence and amount of the obligation without further verification;*
- *If you know, or have a reason to know, that the information on a consumer's credit report is inaccurate, you can ignore it. For example, there might be a fraud alert or a dispute on the credit report, or the consumer may present other evidence that contradicts the credit report. In those cases, you may choose to disregard the inaccurate or disputed items.*

9) How do I verify this information? Here is what the CFPB says:

- *You must use "reasonably reliable third-party records." [For example, you generally cannot rely on what consumers orally tell you about their income. You must verify a consumer's income using documents such as W-2s or payroll statements.];*
- *The rule provides for a wide variety of sources and documents that may help you to verify the information you rely on to determine ATR. You have significant flexibility in how you verify each of the eight factors. For example:*
 - *In addition to a W-2 or payroll statement, you may verify income using tax returns, bank statements, receipts from check-cashing or funds-transfer services, benefits-program documentation, or records from an employer. Copies of tax-return transcripts or payroll statements can be obtained directly from the consumer or from a service provider, and need not be obtained directly from a government agency or employer, as long as the records are reasonably reliable and specific to the individual consumer;*
 - *If a consumer has more income than, in your reasonable and good-faith judgment, is needed to repay the loan, you do not have to verify the extra income. [E.g. if a consumer has both a full-time and a part-time job and you reasonably determine that income from the full-time job is enough for the consumer to be able to repay the loan, you do not have to verify income from the part-time job.];*
 - *You can document a consumer's employment status by calling the employer and getting oral verification, as long as you maintain a record of the information you received on the call;*
 - *You can use a credit report to verify a consumer's debt obligations; you do not need to obtain individual statements for every debt;*
 - *If a consumer does not have a credit history from a credit bureau, you can choose to verify credit history using documents that show nontraditional credit references, such as rental payment history or utility payments.*

10) What are "reasonably reliable third-party records"? The CFPB includes a list of some examples, though it does not purport to be all-inclusive:

- *Records from government organizations such as a tax authority or local government;*
- *Federal, state, or local government agency letters detailing the consumer's income, benefits, or entitlements;*
- *Statements provided by a cooperative, condominium, or homeowners association;*
- *A ground rent or lease agreement;*

- *Credit reports;*
- *Statements for student loans, auto loans, credit cards, or existing mortgages;*
- *Court orders for alimony or child support;*
- *Copies of the consumer's federal or state tax returns;*
- *W-2 forms or other IRS forms for reporting wages or tax withholding;*
- *Payroll statements;*
- *Military leave and earnings statements;*
- *Financial institution records, such as bank account statements or investment account statements reflecting the value of particular assets;*
- *Records from the consumer's employer or a third party that obtained consumer-specific income information from the employer;*
- *Check-cashing receipts;*
- *Remittance-transfer receipts.*

[To be continued]

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