COMMUNITY
Home Lenders Association, Inc.
2101 Wilson Boulevard, Suite 610
Arlington, VA 22201
(571) 527-2601

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CHLA Comment Letter to the CFPB
Docket CFPB-2019-0039
RIN 3170-AA98
Qualified Mortgage Definition under the Truth in Lending Act

The Community Home Lenders Association (CHLA) is pleased to submit these comments in response to the Consumer Financial Protection Bureau (CFPB) Advanced Notice of Proposed Rulemaking (ANPR) regarding the definition of a Qualified Mortgage (QM) and the QM Patch.

This rulemaking raises major questions regarding access to mortgage credit, the importance of an effective Ability to Repay standard for mortgage loans, the reliability of debt-to-income (DTI) ratios in assessing mortgage loan risk, and the importance of Fannie Mae and Freddie Mac purchasing loans that do not meet a strict 43% QM DTI limit.

CHLA is writing to make the following recommendations regarding this rulemaking:

1. **The CFPB should augment any action it takes to extend, replace, or expand the QM Patch by granting the Federal Housing Finance Agency (FHFA) authority to modify that standard for loans purchased by Fannie Mae and Freddie Mac, in order to facilitate a "Utility Model" for Fannie and Freddie for the period after they exit conservatorship.**

2. **The overriding priority for the rulemaking should be for the CFPB to ensure that authority for the GSEs to purchase an estimated $260 billion in annual well-performing loans under the QM Patch shall continue, to ensure adequate access to mortgage credit.**

3. **Proposals to extend the QM Patch to non-GSE loans, such as raising the DTI cap, establishing some benchmark against the Average Prime Offer Rate (APOR), or some combination thereof, may be worthy of consideration; however, a complete elimination of any DTI test should be rejected, due to the risk of a return to subprime era practices.**

Facilitating a GSE Utility Model Through Delegated QM Authority

Momentum appears to be building for a so-called "administrative" approach to reform of the GSEs (Fannie Mae and Freddie Mac). This approach reflects a growing appreciation that most of the necessary major reforms of Fannie and Freddie have already taken place – including among others: (1) Ability to Repay/QM (to end no-doc loans), (2) Credit risk sharing (to shift risk to the private sector and for market discipline), (3) Portfolio wind-downs (to end interest rate risk), (4) a strong regulator (FHFA vs. OFHEO), and (5) Taxpayer compensation for a federal backstop.

The major reform that remains to be accomplished is a recapitalization of Fannie and Freddie, in order to protect taxpayers and operate the GSEs in a more responsible manner and facilitate their exit from conservatorship.

CHLA urges the Treasury Department and the FHFA to work constructively together to develop and carry out a plan to enable Fannie Mae and Freddie Mac to exit conservatorship.

Many parties in Washington, including CHLA, also support a "Utility Model" for GSE reform. This model rejects the chartering of new GSEs to compete with Fannie and Freddie, which would be contrary to a Utility Model, because it encourages the type of race-to-the-bottom behavior to maintain market share that contributed to the GSEs being placed in conservatorship. New charters would also facilitate vertical integration, in which Wall Street banks could use a federal guarantee to deal exclusively with their bank affiliate or to cherry pick the highest FICO score borrowers.

Instead, under a Utility Model, GSEs would act as a securitization conduit for the purchase of loans that meet GSE parameters. This is augmented by: (1) risk sharing that transfers risk to the private sector and (2) a competitive origination market in which thousands of qualified seller-servicers originate loans to GSE standards. This vigorous competition works to the benefit of all consumers.

To make this work, authority would be required for FHFA to regulate the GSEs as a Utility, both to ensure that loan standards meet reasonable standards and to ensure that the GSEs do not take advantage of their duopoly status to overcharge consumers. FHFA, as conservator of the GSEs, appears to have such authority. However, it is doubtful under the Housing and Economic Recovery Act (HERA) that such authority would exist after Fannie and Freddie exit conservatorship.

QM standards deal with precisely these issues. Therefore, the CFPB should grant FHFA the authority to establish different QM standards than it establishes for the broader market. FHFA should have the authority to establish stricter standards than the QM rule the CFPB establishes for types of loans that it concludes represent a safety and soundness concern. And, FHFA should have authority to promulgate more lenient standards for the GSEs in a credit crunch, to ensure adequate consumer mortgage access to credit and to stabilize our nation's housing markets.

Giving FHFA authority to set QM standards for Fannie and Freddie after they exit conservatorship is the best mechanism to ensure that the GSEs meet their statutory access to credit responsibilities, without going off the rails and purchasing risky loans as they did during the subprime crisis.

Critical Importance of Preserving Eligibility for GSE Patch Loans

According to a Core Logic study, Fannie Mae and Freddie Mac purchased $260 billion in loans in 2018 that did not strictly meet QM standards. These loans seem to be performing well, as reflected by the GSEs' consistently strong financial performance. That same study showed that, statistically, these loans play a critical part of an overall mortgage origination market that totals $1.6 trillion.

Therefore, at a minimum, while the CFPB is conducting the rulemaking process, it should provide extensions of the GSE QM patch until a replacement framework is put in place.

As a matter of public policy, it would be entirely reasonable for the CFPB to simply extend the Patch, indefinitely, unless and until the GSEs exit conservatorship. QM is designed to ensure that borrowers have an ability to repay a mortgage loan. As long as the GSEs remain in conservatorship, FHFA has all the authority it needs to ensure that GSE loans are safe and financially responsible. The QM Patch made sense when it was put in place and it would make sense continuing it past its scheduled January 2021 expiration date.

However, CHLA is mindful that the CFPB and the FHFA are interested in extending whatever QM flexibility that is permitted for the GSEs to non-GSE loans. CHLA could support an appropriate replacement QM standard that applies to both GSE loans and non-GSE loans.

Examples of proposals to accomplish this, which CHLA could support, include:

* Modifying the QM 43% DTI cap with authority to go up to 50% potentially with an additional requirement of the loan compensating factors, and with appropriate changes to Appendix Q, or

* Replacing the QM 43% DTI cap for only those loans that meet some proxy standard, such as an appropriate benchmark over Average Prime Offer Rate (APOR).

Regardless of the specific policies CFPB promulgates, the most important priority is to ensure that any such approach preserves the ability of Fannie Mae and Freddie Mac to have authority to continue to make loans currently done as QM Patch loans as QM-eligible loans.

Assuming DTI is retained in some form in a replacement QM standard, CHLA also urges the CFPB to revise Appendix Q. An update of Appendix Q is important to address concerns that there is adequate flexibility for borrowers working in the gig economy with new forms of sporadic employment, as well as providing appropriate flexibility to the self-employed.

Some Consideration of DTI Should Be Retained in a QM Standard

CHLA appreciates that some parties believe that a DTI requirement should be eliminated entirely as part of a re-definition of QM. CHLA is sympathetic to the fact that a strict 43% DTI standard is unduly restrictive and that there are significant numbers of good mortgage loans that exceed this bright line standard. As noted, the GSEs' purchase of loans above the 43% DTI cap bears this out.

The simplest approach to creating a more universal QM definition might be to allow loans up to 50% DTI, potentially in conjunction with a substantive residual income test and/or a demonstration of compensating factors. However, CHLA urges great caution regarding any proposal that would completely eliminate any consideration of DTI for all loans without a suitable proxy.

We note that Congress debated QM standards last year and enacted a targeted exemption from QM for loans originated by smaller banks that are held in portfolio - but did not provide any exemption from QM or the 43% DTI cap for larger banks or private label securities (PLS).

A complete elimination of DTI as a QM factor runs the risk of ignoring the lessons of the subprime era that led to the 2008 housing crisis. We appreciate that such proposals retain the concept of underwriting and documenting income and other product restrictions, such as no-interest or negative-amortization loans. However, a strong documentation of income alone does not appear to meet a reasonable ability to repay standard if DTI levels are excessive.

In recent years, CHLA has vigorously disputed reports that raised alarms about the growth of the non-bank mortgage sector, documenting how such concerns are generally overblown. However, as the only association exclusively representing non-bank IMBs, we must raise concerns about the potential proliferation of large IMBs, REITs and other non-bank entities venturing back into the PLS market, generating risky mortgage loans without any DTI standard.

Therefore, we believe the CFPB should exercise great care in granting QM status to loans that do not meet some reasonable DTI standard.

In closing, CHLA appreciates the opportunity to submit these comments.

Sincerely,

COMMUNITY HOME LENDERS ASSOCIATION