

Qualified Residential Mortgage Rule FAQ

What is a Qualified Residential Mortgage?

A Qualified Residential Mortgage refers to new mortgages that will be created as a result of the Dodd-Frank Act of 2010. In an effort to curb the lax lending standards of banks, the Dodd-Frank Act requires that the federal government develop regulations for Qualified Residential Mortgages (QRM). Under the law, a bank will have to retain an ownership interest in any mortgage it issues if that mortgage does not meet the new requirements of a Qualified Residential Mortgage. Because retaining even a portion of a mortgage would impact a bank's finances, the QRM regulation is likely to have widespread impact. Specifically, it will change the availability and terms of mortgages for home purchases. The goal of developing the QRM standard is to provide strong underwriting requirements and incentives for responsible lending and borrowing. Loans qualifying for QRM status are to be of sufficiently high credit quality so as to reduce the likelihood of borrower default.

What are the Proposed Standards for a QRM?

The draft proposal issued by the federal government would set strict standards for borrowers. To qualify for QRM status borrowers must:

- contribute at least a 20 percent down payment
- pay closing costs out-of-pocket
- provide full documentation of income with strict debt-to-income ratio limitations
- be current on all existing debt payments
- not have been more than 60 days delinquent on ANY debt obligation for the prior 24 months
- not have had any property repossessed within the past 36 months
- not have been a party to a bankruptcy proceeding, foreclosure, a short-sale, or a deed-in-lieu of foreclosure, within the prior 36 months
- not have been subject to a Federal or state judgment for collection of any unpaid debt

What loans and terms are eligible for a QRM?

The proposal limits QRMs to closed-end, first-lien mortgages to purchase a one-to-four-family property that serves as the purchaser's primary residence, or second-liens on refinance transactions only. Adjustable Rate Mortgages are permitted if the annual adjustment is limited to

2 percent in a calendar year and the overall rate may not increase more than 6 percent over the life of the loan. A full written appraisal is also required to qualify for a QRM.

What Loans and Terms are NOT Eligible for a QRM?

Construction loans and reverse mortgages are excluded from the QRM definition. Further, mortgages with a prepayment penalty, a balloon payment, or that allow for negative amortization or interest-only payments are excluded from the standard. The proposed rule also prohibits the practice of “piggyback” mortgages. Also, loan terms greater than 30 years or less than 12 months, and points and fees that exceed 3 percent of the loan balance are excluded from the QRM standard. So called 80-20 loans or 80-15-5 loans where the entire principle is borrowed but broken up to avoid private mortgage insurance requirements are also not allowed under the QRM regulations.

How will QRM Impact the Availability of Mortgages and Mortgage Products?

Because the proposed QRM regulations will impose higher down payment requirements (20 percent), will exclude closing costs from financing and will impose strict limitations on fees and debt-to-income ratios, QRM will likely have a pronounced impact on the availability of mortgages. In fact, a recent study issued by the Federal Housing Finance Agency noted that under the proposed standards only 30 percent of mortgages issued in 2009 would meet the new standards. Thus, if enacted as drafted, the proposed QRM standard will limit the pool of potential buyers which in turn will further depress the housing market.

Does QRM set any Underwriting Requirements for Community Associations?

No, unlike the Federal Housing Administration’s (FHA) Condominium Insurance Guidelines, the QRM regulation criteria focus on borrower and lender requirements. However, the QRM regulations require that when calculating the mortgage payment, to determine if the borrower qualifies for a mortgage, must factor in any community association assessments into the final payment, and the final payment must not exceed a certain percentage of a borrower’s income. This would benefit community associations by ensuring that purchasers not only could afford the mortgage, but also any required association assessments.

What if I do not Qualify for a QRM?

Borrowers who are unable to meet the requirements established under the QRM regulations, will be forced into low-income borrow programs such as those offered by the FHA or into mortgage products provided by the private sector (if any). Critics of the proposal from the mortgage industry indicate that private, market driven products for borrowers not meeting the QRM criteria could carry an interest rate of up to 3 percent more than qualifying mortgages.

What is the Status of the Proposed QRM Regulation?

The agencies released a joint proposed rule to implement the risk retention requirements of the Dodd-Frank Act on March 30, 2011. Among agency discussion and justification for the decisions taken in crafting the proposed rule, the proposed rule seeks public comment on 174 issues. Public comment on the proposed rule must be received by June 10, 2011. CAI will be submitting comments and will work on a comment template for our members.

What has CAI Accomplished in Respect to the Rule Making Process?

Because these regulations, when finalized, will have a fundamental impact on all mortgage lending, CAI reached out to the seven federal agencies before the regulatory process even began. We did so to express concerns and recommendations on how such regulations would impact the 64 million Americans who live in community associations. You can read that letter [here](#).

On January 11, 2011, CAI signed on to a letter urging the federal government to take a studied approach to overhauling the mortgage finance system. The industry letter was signed by a diverse group of housing, consumer and mortgage related organizations including CAI, the National Association of Homebuilders, The National Association of Realtors, Asian Real Estate Association of America, Center for Responsible Lending, Community Mortgage Banking Project, Community Mortgage Lenders of America, Consumer Federation of America, Mortgage Bankers, Mortgage Insurance Companies of America, National Association of Real Estate Brokers and the American Land Title Association. You can read the letter [here](#).

CAI will continue to monitor the development of the QRM standard and ensure that the perspective of community associations is heard through the rule making process.

CAI is also giving careful consideration and closely monitoring a balance in the underwriting requirements and the availability of credit. The agencies believe a narrowly defined QRM will induce lenders to originate and foster a secondary market for these loans. If the agencies' assumptions are correct and a secondary market develops, QRMs might experience similar pressure as FHA did in 2003 through 2007, where FHA's market share fell to less than 2 percent. Allowing the secondary market to set mortgage terms will mean homeowners pay a higher risk premium for loans that have more flexible underwriting; however, homeowners will also be exposed to lender flight in a troubled economy. If a broad definition is adopted the government will set underwriting standards for most of the mortgage market. Meaning all homeowners will have to put more into a mortgage transaction (higher down payment, closing costs, etc.) and be subject to government regulation.

If you have any questions on the QRM proposal and how it could affect your community, email government@caionline.org with QRM Proposal in the subject line.