March 2016

Ability-to-Repay and Qualified Mortgage Rule

Small entity compliance guide

Consumer Financial Protection Bureau

Version log

The Bureau updates this guide on a periodic basis to reflect rule changes and administrative updates which impact guide content. Below is a version log noting the history of this document and its updates:

Date	**Version**	**Rule Changes**
March 28, 2016	2.4	The Bureau issued a final rule, the September 2015 Final Rule, amending certain mortgage rules,and the March 2016 Interim Final Rule to ▪ Revise the definitions of small creditor and rural area. ▪ Amend the requirements to make QM's for small creditors ▪ Establish a grace period to allow a creditor that does not meet the small creditor origination limit or asset limit in the preceding year to operate as a small creditor for mortgage transactions with applications received before April 1 of the current calendar year if it meets the limits in the calendar year before the preceding calendar year. ▪ Establish a grace period to allow a small creditor that did not meet the test for operating in a rural or underserved area in the preceding calendar year to operate as a small rural creditor for mortgage transactions with applications received prior to April 1 of the current calendar year if it met the rural or underserved test in the calendar year before the preceding calendar year. (See "*What type of QMs can small creditor originate?*" on page 38)

		Temporary QM Provision. The Federal Housing Administration (FHA) and the U.S. Department of Veterans Affairs (VA) have each issued their own QM rules. Therefore, the section of the guide that addresses this has been modified. (See "*Type 2: Temporary QM definition*" on page 37)
November 3, 2014	2.3	The Bureau published a final rule amending certain mortgage rules to ▪ amend the existing exemption from the ability-to-repay rule for nonprofit entities that meet certain requirements(*See "Which types of creditors and loan programs are exempt from the ability-to-repay requirements?" on page 30),* ▪ provide a cure mechanism for the points and fees limit that applies to qualified mortgages (*See "What are the QM points-and-fees caps and what do I include when calculating points and fees?" on page 43*)
January 8, 2014	2.2	Miscellaneous Administrative Changes
October 17, 2013	2.1	*Points-and-Fees Calculation: Loan Originator Compensation.* Clarifies for retailers of manufactured homes and their employees what compensation must be counted as loan originator compensation and thus included in the points and fees thresholds for qualified mortgages and high-cost mortgages. (*See "What are the QM points-and-fees caps and what do I include when calculating points and fees?' on page 43.)* ▪ *Points and Fees Calculation: Non-consumer payments.* Clarifies the treatment of payments made by the creditor or a seller or other third party,

		rather than by the consumer, for purposes of what must be included in the points and fees thresholds for qualified mortgages and high-cost mortgages. *(See "What are the QM points-and-fees caps and what do I include when calculating points and fees? on page 43.)* *Period to be considered when making Small Creditor status determination after January 10, 2016.* Changes the look back period for rural and underserved lending activity that is used in the definition of Small Creditor, effective January 10, 2016. (*See "What types of QMs can small creditors originate?" Type 2: Balloon-Payment QM on page 40.*)
August 14, 2013	2.0	*Exemptions:* Creditors with certain designations, loans pursuant to certain programs, certain nonprofit creditors, and mortgage loans made in connection with certain Federal emergency economic stabilization programs are exempt from ability to repay requirements. *(See "Which types of creditors and loan programs are exempt from the ability-to-repay requirements?" on page 30.)* *Qualified Mortgages (QMs):* Additional definition of a qualified mortgage for loans held in portfolio by small creditors. *(See "What types of QMs can small creditors originate?" on page 38.)* *Qualified Mortgages:* Transitional definition of creditors eligible to originate Balloon-Payment Qualified Mortgages. *(See "What types of QMs can small creditors originate?" on page 38.)* *Qualified Mortgages:* Shifts the annual percentage rate (APR) threshold for Small Creditor and Balloon-Payment QMs from 1.5 percentage points above the average prime

		offer rate (APOR) on first-lien loans to 3.5 percentage points above APOR. *(See "What makes a QM loan higher-priced?" on page 34.)* *Points-and-Fees Calculation:* Modifies the requirements regarding the inclusion of loan originator compensation in the points-and-fees calculation. *(See "What are the QM points-and-fees caps and what do I include when calculating points and fees?" on page 43.)* *Qualified Mortgages:* Clarifies how eligibility will be determined for QMs under the temporary provision allowing QM status for loans eligible for purchase, guaranty, or insurance by the GSEs or certain federal agencies. *(See "What types of QMs can all creditors originate? Type 2 on page 37.)* *Qualified Mortgages:* Amends and clarifies how debt and income will be determined under appendix Q for the purpose of meeting the 43% DTI requirement under the general QM provision. *(See "What types of QMs can all creditors originate? Type 1" on page 36).*
April 30, 2013	1.0	Original Document

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1. Introduction

During the years preceding the mortgage crisis, too many mortgages were made to consumers without regard to the consumers' ability to repay the loans. Loose underwriting practices by some creditors – including failure to verify consumers' income or debts and qualifying consumers for mortgages based on "teaser" interest rates after which monthly payments would jump to unaffordable levels – contributed to a mortgage crisis that led to the nation's most serious recession since the Great Depression.

In response to this crisis, in 2008 the Board of Governors of the Federal Reserve System adopted a rule under the Truth in Lending Act prohibiting creditors from making higher-priced mortgage loans without assessing consumers' ability to repay the loans. Creditors have had to follow these requirements since October 2009.

In the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), Congress adopted similar (but not identical) Ability-to-Repay (ATR) requirements for virtually all closed-end residential mortgage loans. Congress also established a presumption of compliance with the ATR requirements for a certain category of mortgages, called Qualified Mortgages (QMs).

In January 2013, the Consumer Financial Protection Bureau adopted a rule that implements the ATR/QM provisions of the Dodd-Frank Act. In May, July, and October 2013 and in October 2014, the Bureau issued rules amending certain provisions of the January 2013 rule. In September 2015 and March 2016, the Bureau issued rules further amending the ATR/QM rule's small creditor provisions. The ATR/QM rule is the subject of this guide.

This rule generally applies to closed-end consumer credit transactions that are secured by a dwelling for which you receive an application on or after January 10, 2014.

As you will see in reading this guide, the ATR rule describes the minimum standards you must use to determine that consumers have the ability to repay the mortgages they are extended.

While the ATR rule provides eight specific factors you must consider (including verifications of income or assets relied on, employment if relied on, and review of credit history), the rule does not dictate that you follow particular underwriting models.

The rule also contains special requirements for creditors that are refinancing their own customers into more affordable loans to help those customers avoid payment shock.

In addition to the general ATR requirements, the rule also defines the requirements for Qualified Mortgages and how QM status works if there is a question about whether a creditor has assessed the borrower's ATR.

The rule provides a safe harbor for QMs that are not higher-priced. Loans that are higher-priced and meet the definition of a Qualified Mortgage have a different protection, that of a rebuttable presumption that the creditor complied with the ATR requirements.

This guide explains the requirements for creditors to follow to determine whether the loans your organization originates meet the QM requirements and, if so, whether they will receive either a safe harbor or rebuttable presumption of compliance with the ATR requirements.

It also discusses the grounds for rebutting the presumption for higher-priced QMs – principally, that the consumer's income, debt obligations, and payments on the loan and any simultaneous loans – did not leave the consumer with sufficient residual income/assets left to live on.

Qualified Mortgages have three types of requirements: restrictions on loan features, points and fees, and underwriting. One of the underwriting requirements under the general definition for Qualified Mortgages is that the borrower's total debt-to-income ratio is not higher than 43 percent.

For a temporary, transitional period, certain loans that are eligible for sale or guarantee by a government-sponsored enterprise (GSE) – the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac) – or are eligible under specified federal agencies' guarantee or insurance programs will be considered Qualified Mortgages under a temporary definition. The loans must meet certain QM restrictions on loan features and points and fees, but they are not subject to a flat 43 percent DTI limit.

In response to the special concerns of small creditors and to preserve access to nonconforming mortgages and mortgages in rural and underserved areas, there are also special provisions for

Qualified Mortgages held in portfolio by small creditors, including some types of balloon-payment mortgages. These Qualified Mortgages have a different, higher threshold for when they are considered higher-priced for Qualified Mortgage purposes than other Qualified Mortgages. They also are not subject to the 43 percent DTI limit.

Finally, the rule bans most prepayment penalties, except on certain non-higher-priced Qualified Mortgages with either fixed or step rates. Prepayment penalties are allowed on these non-higher-priced loans only if the penalties satisfy certain restrictions and are permitted under law and if the creditor has offered the consumer an alternative loan without such penalties.

1.1 What is the purpose of this guide?

The purpose of this guide is to provide an easy-to-use summary of the ATR/QM rule. This guide also highlights issues that small creditors, and those that work with them, might find helpful to consider when implementing the rule.

This guide also meets the requirements of Section 212 of the Small Business Regulatory Enforcement Fairness Act of 1996, which requires the Bureau to issue a small-entity compliance guide to help small businesses comply with new regulations.

The guide summarizes the ATR/QM rule, but it is not a substitute for the rule. Only the rule and its Official Interpretations (also known as Commentary) can provide complete and definitive information regarding its requirements. The discussions below provide citations to the sections of the rule on the subject being discussed. Keep in mind that the Official Interpretations, which provide detailed explanations of many of the rule's requirements, are found after the text of the rule and its appendices. The interpretations are arranged by rule section and paragraph for ease of use. The complete rule, as issued on January 10, 2013 and the Official Interpretations are available at http://www.consumerfinance.gov/regulations. Additionally, the Bureau has issued four final rules and an interim final rule to amend and clarify provisions in the January 2013 Final Rule: the June 2013 ATR/QM Concurrent Final Rule, July 2013 Final Rule, October 2013 Final Rule, November 2013 Final Rule, September 2015 Final Rule, and March 2016 Interim Final Rule.

The focus of this guide is the ATR/QM rule. This guide does not discuss other federal or state laws that may apply to the origination of closed-end credit.

At the end of this guide, there is more information about the rule and related implementation support from the Bureau.

1.2 Who should read this guide?

If your organization originates closed-end residential mortgage loans, you may find this guide helpful. This guide will help you determine your compliance obligations for the mortgage loans you originate.

This guide may also be helpful to secondary market participants, software providers, and other companies that serve as business partners to creditors.

1.3 Where can I find additional resources that will help me understand the ATR/QM rule?

Resources to help you understand and comply with the Dodd-Frank Act mortgage reforms and our regulations, including downloadable compliance guides, are available through the CFPB's website at www.consumerfinance.gov/regulatory-implementation. If after reviewing these materials you have a specific ATR/QM regulatory interpretation question, submit a detailed message, including your name, contact information, details about your regulatory question, and the specific title, section, or subject matter of the regulation you are inquiring about, to CFPB_RegInquiries@cfpb.gov. If you do not have access to the internet, you may leave this information in a voicemail at 202-435-7700. Please note that Bureau staff provide only an informal oral response to regulatory inquiries and that the response does not constitute an official interpretation or legal advice. Generally we are not able to respond to specific inquiries the same business day. Actual response times will vary depending on the number of questions we are handling and the amount of research needed to respond to your question.

Email comments about the guide to CFPB_MortgageRulesImplementation@cfpb.gov. Your feedback is crucial to making this guide as helpful as possible. The Bureau welcomes your suggestions for improvements and your thoughts on its usefulness and readability.

The Bureau is particularly interested in feedback relating to:

- How useful you found this guide for understanding the rule
- How useful you found this guide for implementing the rule at your business
- Suggestions you have for improving the guide, such as additional implementation tips

2. Overview of the Ability-to-Repay/Qualified Mortgage Rule

2.1 What is the ATR/QM rule about?

The ATR/QM rule requires 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

The rule also requires you to consider and verify the consumer's credit history.

As discussed in more detail below, the rule provides a presumption that you have complied with the ATR rule if you originate QMs.

QMs generally cannot contain certain risky features (such as allowing interest-only payments or negative amortization). In addition, points and fees on QMs are limited. For a loan to be a QM, it also must meet certain underwriting criteria.

In exchange for meeting these requirements, QMs receive either a conclusive or a rebuttable presumption that you, the creditor, complied with the ATR requirements. The type of presumption depends on the pricing of the loan - whether the loan is not higher-priced or is higher-priced.

The ATR/QM rule also implements other provisions of the Dodd-Frank Act that:

- Limit prepayment penalties
- Require that you retain records for three years after consummation showing you complied with ATR and other provisions of this rule

2.2 When do I have to start following this rule?

The ATR-QM rule generally took effect on January 10, 2014. The Bureau will – from time to time – issue rule updates that have different effective dates.

The Truth in Lending Act applies to a loan modification only if it is considered a refinancing under Regulation Z. If a loan modification is not subject to the Truth in Lending Act, it is not subject to the ATR/QM rule. Therefore, you should determine if a loan modification is a refinancing to see if the ATR/QM rule applies. You will find the rules for determining whether a loan workout is a modification or a refinance in Regulation Z at § 1026.20(a) and accompanying Commentary.

The Bureau's ATR/QM rule applies to 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. Unlike some other mortgage rules, the ATR/QM rule is not limited to first liens or to loans on primary residences.

However, some specific categories of loans are excluded from the rule. Specifically, the rule **does not apply to:**

- Open-end credit plans (home equity lines of credit, or HELOCs)
- Time-share plans
- Reverse mortgages
- 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. *(See "Which types of creditors and loan programs are exempt from the ability-to-repay requirements?" on page 30.)*

2.3 How long do I have to keep records on compliance with the ATR/QM rule? (§ 1026.25(c)(3))

The rule requires that you retain evidence that you complied with the ATR/QM rule, including the prepayment penalty limitations, for three years after consummation, though you may want to keep records longer for business purposes.

3. About Ability to Repay

3.1 What is the general ATR standard? (Comment 1026.43(c)(1)-2)

Under the general ATR standard, you must make a reasonable, good-faith determination before or when you consummate a covered mortgage loan that the consumer has a reasonable ability to repay the loan.

3.2 What are the eight ATR underwriting factors I must consider and verify under the rule? (Comment 1026.43(c)(2)-4)

A reasonable, good-faith ATR evaluation must include eight ATR underwriting factors:

1. Current or reasonably expected income or assets (other than the value of the property that secures the loan) that the consumer will rely on to repay the loan

2. Current employment status (if you rely on employment income when assessing the consumer's ability to repay)

You may already have underwriting policies, procedures, and internal controls that consider these factors. However, you should check your policies and procedures to ensure that they reflect that you will consider each of the eight factors. It may also be helpful to document how you consider the factors. However, the rule does not require validation of underwriting criteria using mathematical models.

3. Monthly mortgage payment for this loan. You calculate this using the introductory or fully-indexed rate, whichever is higher, and monthly, fully-amortizing payments that are substantially equal (*See "What do I include on the debt side of the debt-to-income ratio when determining ATR?" on page 25 for special rules for calculating payments for interest-only, negative-amortization, and balloon loans*.)

4. Monthly payment on any simultaneous loans secured by the same property

5. 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

6. Debts, alimony, and child-support obligations

7. 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

8. Credit history

The rule does not preclude you from considering additional factors, but you must consider at least these eight factors.

3.3 How do I verify information I considered using reliable third-party records? (Comment 1026.43(c)(3)-4)

Your organization must verify the information you rely on using 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.

While you must follow the reasonably reliable third-party standard, the rule provides for a wide variety of sources that may help you to verify the information you rely on to determine ATR.

There are a wide variety of documents and sources of information your organization can use as you determine ATR, and 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.

While you do not have to retain actual paper copies of documentation used in underwriting a transaction, you must be able to reproduce such records accurately. For example, if you use a consumer's W-2 tax form to verify income, you must be able to reproduce the form itself, not merely the income information that was contained in the form. Accordingly, you can obtain records transmitted electronically, such as via email or a secure external Internet link to access information, if you can retain or otherwise reproduce such records accurately during the three years you must retain ATR records. (Comment 43(b)(13)-1)

- 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. For example, 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.

3.4 What is a reasonably reliable third-party record? (§ 1026.43(c)(3))

Here is a list of some of the types of reasonably reliable third-party records your organization may choose to use. Note, however, that this list is not 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

When determining ATR, you have to verify only the income or assets used to qualify the consumer for the loan.

When the consumers' applications list debt that does not show up on their credit reports, you must consider that debt in assessing either the consumers' debt-to-income ratios or residual income, but you do not need to independently verify that debt.

- Remittance-transfer receipts

3.5 How do I determine ATR? (§ 1026.43(c)(1))

Your organization is responsible for developing and applying its own underwriting standards and making changes to those standards over time in response to empirical information and changing economic and other conditions.

To help your organization incorporate the ATR concepts into its operations, the Bureau has prepared some examples that illustrate how your internal policies can influence your ATR determinations.

The list below is **not** a comprehensive list of all the ways your underwriting guidelines might measure ATR.

Each of you must look at the issue of ATR in the context of the facts and circumstances relevant to your market, your organization, and your individual consumers.

Given those caveats, here are some of the types of factors that may show that your **ATR determination was reasonable and in good faith**:

- Underwriting standards: You used standards to underwrite the transaction that have historically resulted in comparatively low rates of delinquency and default during adverse economic conditions.
- Payment history: The consumer paid on time for a significant time after origination or reset of an adjustable-rate mortgage.

Among the types of factors that may show that your ATR determination was not reasonable and in good faith:

- Underwriting standards: You ignored evidence that your underwriting standards are not effective at determining consumers' repayment ability.

- Inconsistency: You applied underwriting standards inconsistently or used underwriting standards different from those you used for similar loans without having a reasonable justification.
- Payment history: The consumer defaults early in the loan, or shortly after the loan resets, without having experienced a significant financial challenge or life-altering event.

The reasonableness and good faith of your determination of ATR depends on the facts and circumstances relevant to the particular loan. For example, a particular ATR determination may be reasonable and in good faith even though the consumer defaulted shortly after consummation if, for example, the consumer experienced a sudden and unexpected loss of income.

If the records you review indicate there will be a change in the consumers' repayment ability after consummation (for example, they plan to retire and not obtain new employment, or they plan to transition from full-time to part-time work) you must consider that information. (Comment 43(c)(1)-2) However, you may not make inquiries or verifications prohibited by Regulation B. (Comment 43(c)(1)-3)

3.6 Do loans originated under the general ATR standard have to comply with a debt-to-income (DTI) threshold? (§ 1026.43(c)(2)(vii))

The general ATR standard requires creditors to consider DTI or residual income, but does not contain specific DTI or residual income thresholds.

3.7 What do I include on the income side of the debt-to-income ratio when determining ATR?

You can include earned income (wages or salary); unearned income (interest and dividends); and other regular payments to the consumer such as alimony, child support, or government benefits. In all cases, the amounts you rely upon to determine ATR must be verified.

Once you have information about the consumers' income, you will use it, along with the consumers' debt information, to calculate the DTI ratio or residual income.

3.8 How do I calculate, consider, and confirm income, assets, employment, and credit history?

When you are evaluating the consumer's employment history, credit history, and income or assets to determine ATR, you must verify only what is relied on to determine ATR.

If a consumer has a full-time job and a part-time job and uses only the income from the full-time job to pay the loan, you do not need to verify the income from the part-time job. If two or more consumers apply for a mortgage, you do not have to consider both incomes – unless both incomes are required to qualify for the loan and demonstrate ATR.

The same principles apply to a consumer's assets, too.

Income does not have to be full-time or salaried for you to consider it in your ATR determination. You can consider seasonal or bonus income. Remember that income relied on has to be verified using reasonably reliable third-party records.

For example, you could verify a Christmas tree farmer's seasonal income via tax returns showing that the farmer earned $50,000 a year during the past three Decembers and nothing else the rest of the year, and divide that $50,000 evenly across 12 months.

Future income can count toward ATR if you verify it using reasonably reliable third-party records. Suppose you have a consumer who accepts a job in March, but will not start until he graduates from school in May. If the employer will confirm the job offer and salary in writing, you can consider the future expected income in your ATR determination.

3.8.1 Consumer-supplied income documents (§ 1026.43(b)(13))

Sometimes you may have to rely on the consumers' report of their own income. For example, a cattle rancher might give you an updated profit-and-loss statement for the current year to supplement his tax returns from prior years. These records are reasonably reliable third-party records to the extent that an appropriate third party has reviewed them. For example, if a third-party accountant prepared or reviewed the cattle rancher's profit-and-loss statement, then you can use the statement to verify the rancher's current income.

3.8.2Types of employment information (§ 1026.43(c)(3))

You can consider and verify many types of employment to use in making your ATR determination, including:

- Full-time
- Part-time
- Seasonal
- Irregular
- Military
- Self-employment

Consider the characteristics of the consumer's type of employment. A wheat farmer has a different income stream than a store clerk.

You can verify the consumer's employment by calling the employer and obtaining oral verification, so long as you make a written record memorializing the verification.

3.8.3 Sources of credit history information (§ 1026.43(c)(3)(iii))

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.

3.9 What do I include on the debt side of the debt-to-income ratio when determining ATR?

In assessing a consumer's ATR, four underwriting factors help you evaluate the consumer's debts. You will need to find out the consumer's total monthly payments for:

1. The loan you are underwriting
2. Any simultaneous loans secured by the same property
3. Mortgage-related obligations – property taxes; insurance required by the creditor; fees owed to a condominium, cooperative, or homeowners association; ground rent or leasehold payments; and special assessments
4. Current debt obligations, alimony, and child support

Once you have the total debt figure, you will use it, along with the consumer's total monthly income, to calculate the monthly debt-to-income ratio or residual income.

Include ongoing, required monthly, quarterly, or annual debts of the consumer.

Do not include debts paid off at or before consummation.

3.10 How do I calculate, consider, and confirm debt information

3.10.1 Calculating payments under the ATR standard for the loan you are underwriting: (§ 1026.43(c)(5))

General rule: If the interest rate on the loan can vary during the term of the loan, as with an adjustable-rate or step-rate mortgage, when you calculate the monthly payment the consumer will have to make for the new loan, you will usually use the greater of the fully-indexed rate or the introductory rate.

You must base your calculations on substantially equal monthly payments that would fully amortize the loan

Special rules: However, there are also special rules and guidance provided for certain types of loans:

- For balloon loans, the calculation depends on whether the loan is a higher-priced loan. Higher-priced loans are generally defined as having an annual percentage rate (APR) that, as of the date the interest rate is set, exceeds the Average Prime Offer Rate (APOR) by 1.5 percentage points or more for first-lien loans and 3.5 percentage points or more for subordinate-lien loans. APOR is published weekly at https://www.ffiec.gov/ratespread.
- For non-higher-priced balloon loans: Use the maximum payment scheduled during the first five years after the first regular periodic payment comes due.
- For higher-priced balloon loans: Use the maximum payment in the payment schedule, including any balloon payment.
- For interest-only loans: Use the greater of the fully-indexed or introductory rate and equal, monthly payments of principal and interest that will repay the outstanding loan amount on the date the loan recasts over the remaining term of the loan.
- For negative-amortization loans: Calculate the maximum loan amount, which will include the potential added principal assuming the consumer makes the minimum required payments until the date the loan recasts. Use the greater of the fully-indexed or introductory rate and equal, monthly payments of principal and interest that will repay that maximum loan amount on the date the loan recasts over the remaining term of the loan.

To be **substantially equal**, no two monthly payments should vary by more than 1 percent. For loans paid quarterly or annually, convert the payments into monthly payments when you determine ATR.

3.10.2 Calculating payments for simultaneous loans secured by the same property: (§ 1026.43(c)(6))

A simultaneous transaction, such as a piggy-back or silent second, can influence a consumer's ATR. A transaction that recently closed or will close around the same time as the mortgage you are originating may not show up on the consumer's credit report.

But if you know, or have reason to know, that there is going to be a simultaneous transaction around the time your transaction consummates, you need to consider the monthly payment on that transaction in accordance with the following requirements.

- For simultaneous transactions that are not HELOCs - Your ATR assessment should include a monthly payment on the simultaneous loan that is calculated using the appropriate calculation method for adjustable-rate mortgages, interest-only loans, or other categories discussed above, depending on what type of simultaneous loan is made.
- For simultaneous transactions that are HELOCs - Your ATR assessment should include a monthly payment on the simultaneous loan that is calculated based on the amount of credit to be drawn down at or before consummation of the main loan.

3.10.3 Mortgage-related obligations: (§ 1026.43(c)(3) and comment 43(c)(3)-5)

You can get records for the consumer's mortgage-related obligations from many sources including:

- Property taxes: government entities or the amount listed on the title report (if the source of the information was a local taxing authority)
- Cooperative, condominium, or homeowners associations: a billing statement from the association
- Levies and assessments: statement from the assessing entity (for example, a water district bill)
- Ground rent: the current ground rent agreement
- Lease payments: the existing lease agreement

- Other records: can be reasonably reliable if they come from a third party

3.10.4 Other recurring debts: (§ 1026.43(c)(3) and comment 43(c)(3)-6)

The rule requires you to consider a consumer's current debt obligations and any alimony or child support the consumer is required to pay.

Typical recurrent monthly **debts** include:

- Student loans
- Auto loans
- Revolving debt
- Existing mortgages not being paid off at or before consummation

You can generally verify such obligations based on the consumer's credit report or based on other items reported on the consumer's application. Creditors have significant flexibility to consider current debt obligations in light of facts and circumstances, including that an obligation is likely to be paid off soon after consummation. Similarly, creditors should consider whether debt obligations in forbearance or deferral at the time of underwriting are likely to affect the consumer's ability to pay after the expiration of the forbearance or deferral period. (*See discussion on page 24 regarding when it is appropriate to disregard information in a credit report because it is disputed or inaccurate*.)

When two or more customers apply as joint obligors with primary liability on a loan, consider the debt obligations and credit histories of both of them in assessing their ability to repay the loan. But you do not have to include in your ATR consideration the debt obligations or credit history of someone who is merely a guarantor or surety on the loan. (Comment 43(c)(2)(vi)-2)

3.11 Does the ATR rule ban certain loan features or transaction types? (§ 1026.43(c)(2) and (5))

The ATR rule does not ban any particular loan features or transaction types, but a particular loan to a particular consumer is not permissible if the creditor does not make a reasonable, good-faith determination that the consumer has the ability to repay. Thus, the rule helps ensure underwriting practices are reasonable.

For example, it will no longer be possible to originate loans based on stated income. You must now verify the consumer's income or assets and employment relied on in order to comply with the ATR rule.

Likewise, the rule also requires you to underwrite loans with nontraditional features, such as interest-only or negative-amortization periods, by considering the consumer's ability to repay the loan after the initial period.

For higher-priced balloon loans that do not meet the requirements of a balloon-payment QM, you will need to underwrite the balloon payment itself, though balloon loans that are not higher-priced do not have this requirement.

3.12 What happens if a consumer has trouble repaying a loan I originate under the general ATR rule? What happens if my organization violates the regulation?

Whether or not you complied with the ATR requirements is based on the information available during origination.

For example, you are not in violation of the ATR requirements if consumers cannot repay their mortgage loans solely because they experienced a sudden and unexpected job loss after you originated the loan. The ATR determination applies to information known at or before consummation.

However, if consumers have trouble repaying a loan you originate, they could claim that you failed to make a reasonable, good-faith determination of their ATR before you made the loan. If the consumers prove this claim in court, you could be liable for, among other things, up to three years of finance charges and fees the consumers paid as well as the consumers' legal fees.

There is a three-year statute of limitations on ATR claims brought as affirmative cases. After three years, consumers can bring ATR claims only as setoff/recoupment claims in a defense to foreclosure.

3.13 Which types of creditors and loan programs are exempt from the ability-to-repay requirements? (§ 1026.43(a)(3)(iv) to (vi))

Extensions of credit made by certain types of creditors are exempt from the ATR requirements.

- Extensions of credit made by creditors designated by the U.S. Department of the Treasury as Community Development Financial Institutions and creditors designated by HUD as either a Community Housing Development Organization or a Downpayment Assistance Provider of Secondary Financing are exempt from the ATR requirements, under certain conditions.

- Extensions of credit made by creditors designated as nonprofit organizations under section 501(c)(3) of the Internal Revenue Code of 1986 that extend credit no more than 200 times annually, provide credit only to low-to-moderate income consumers, and follow their own written procedures to determine that consumers have a reasonable ability to repay their loans are also generally exempt from the ATR requirements. Note that some subordinate liens are not counted towards the 200-credit extension limit. *See* § 1026.43(a)(3)(vii).

Extensions of credit made pursuant to certain loan programs are exempt from the ATR requirements.

- Extensions of credit made by housing finance agencies directly to consumers, as well as extensions of credit made by other creditors pursuant to a program administered by a housing finance agency, are exempt from the ATR requirements. This ATR exemption applies to extensions of credit made pursuant to a program administered by a housing finance agency, regardless of the funding source (e.g., Federal, State, or other sources).
- Extensions of credit made pursuant to an Emergency Economic Stabilization Act program, such as extensions of credit made pursuant to a State Hardest Hit Fund program, are also exempt from the ATR requirements.

The exemptions above apply to all loans made by these creditors or pursuant to these loan programs, provided the conditions for the exemption are satisfied. An exempt loan remains exempt even if it is sold, assigned, or otherwise transferred to a creditor that would not qualify for the exemption.

Note that the ATR requirements **do not apply** to these loans. Thus, a loan that is eligible for one of these exemptions is not eligible for QM status, as the QM provisions are only applicable to loans subject to the ATR requirements. A consumer who obtained a loan that was exempt from the ATR requirements would have no ability-to-repay claim under the ATR/QM rule.

Please note that although these loans are not subject to the ATR requirements, they still are subject to the restrictions on prepayment penalties discussed on page 49 and may not be structured as open-end credit plans to evade those restrictions.

4. About Qualified Mortgages

4.1 What is a Qualified Mortgage? (§ 1026.43(e) and (f))

The rule provides a presumption that creditors that originate Qualified Mortgages (QMs) have complied with the ATR requirements. That means a court will treat a case differently if a consumer files an ATR claim where the loan is a QM. Creditors will be presumed to have complied with the ATR requirements if they issue QMs. The QM standard helps protect consumers from unduly risky mortgages. It also gives you more certainty about potential liability.

There are four types of Qualified Mortgages under the rule. Two types, the General and Temporary QM definitions, can be originated by all creditors. Two other types, Small Creditor and Balloon-Payment QMs, can only be originated by small creditors. *(See "Are there different types of QMs?" on page 35.)*

The QM requirements generally focus on prohibiting certain risky features and practices, such as negative amortization and interest-only periods and loan terms longer than 30 years.

In addition, for all types of QMs, points and fees generally may not exceed 3 percent of the total loan amount, but higher thresholds are provided for loans below $100,000. *(See "What are the QM points-and-fees caps and what do I include when calculating points and fees?" on page 43.)*

The type of presumption of compliance for a QM depends on whether it is **higher-priced**. Qualified Mortgages under the General and Temporary definitions are considered higher-priced if they have an APR that exceeds the APOR by 1.5 percentage points or more for first-lien loans and 3.5 percentage points or more for subordinate-lien loans. Small Creditor and Balloon-

Payment QMs are considered higher-priced if they have an APR that exceeds the APOR by 3.5 percentage points or more for both first-lien and subordinate-lien loans. *(See "What makes a QM loan higher-priced?" on page 34.)*

If a loan that is **not higher-priced** satisfies the QM criteria, a court will conclusively presume that you complied with the ATR rule.

If a **higher-priced** loan meets the QM criteria, a court will presume it complies with the ATR requirements, but the consumer may rebut the presumption.

4.2 What is the difference between safe harbor and rebuttable presumption in terms of liability protection? (§ 1026.43(e)(1))

QMs can receive two different levels of protection from liability. Which level they receive depends on whether the loan is higher-priced or not. (*See "What makes a QM loan higher-priced?" on page 34*.)

4.2.1 Safe harbor

QMs that **are not higher-priced** have a safe harbor, meaning that they are conclusively presumed to comply with the ATR requirements.

Under a **safe harbor**, if a court finds that a mortgage you originated was a QM, then that finding conclusively establishes that you complied with the ATR requirements when you originated the mortgage.

For example, a consumer could claim that in originating the mortgage you did not make a reasonable and good-faith determination of repayment ability and that you therefore violated the ATR rule. If a court finds that the loan met the QM requirements and was not higher-priced, the consumer would lose this claim.

The consumer could attempt to show that the loan is not a QM (for example, under the General QM definition that the DTI ratio was miscalculated and exceeds 43 percent), and therefore is not presumed to comply with the ATR requirements. However, if the loan is indeed a QM and is not higher-priced, the consumer has no recourse under this regulation.

4.2.2 Rebuttable presumption

QMs that **are higher-priced** have a rebuttable presumption that they comply with the ATR requirements, but consumers can rebut that presumption.

Under a **rebuttable presumption**, if a court finds that a mortgage you originated was a higher-priced QM, a consumer can argue that you violated the ATR rule. However, to prevail on that argument, the consumer must show that based on the information available to you at the time the mortgage was made, the consumer did not have enough residual income left to meet living expenses after paying their mortgage and other debts.

The rebuttable presumption provides more legal protection and certainty to you than the general ATR requirements, but less protection and certainty than the safe harbor.

4.3 What makes a QM loan higher-priced? (§ 1026.43(b)(4))

A Qualified Mortgage under the General or Temporary definition is **higher-priced** if:

- It is a first-lien mortgage for which, at the time the interest rate on the loan was set, the APR was 1.5 percentage points or more over the Average Prime Offer Rate (APOR).
- It is a subordinate-lien mortgage with an APR that, when the interest rate was set, exceeded the APOR by 3.5 percentage points or more.

For example, if the APOR is 5 percent at the time when the interest rate on a mortgage is set, then a first-lien mortgage is higher-priced if it has an APR of 6.5 percent or more.

A Small Creditor or Balloon-Payment QM is higher-priced if:

- It has an APR that, when the interest rate was set, exceeded the APOR by 3.5 percentage points or more, for both first-lien and subordinate-lien mortgages.
- For example, if the APOR is 5 percent at the time when the interest rate on a mortgage is set, a mortgage that is a Small Creditor Qualified Mortgage is higher-priced if it has an APR of 8.5 percent or more, regardless of whether it is first- or subordinate-lien loan.

This special definition of higher-priced for Small Creditor and Balloon-Payment QMs only determines whether a loan has a safe harbor or rebuttable presumption of compliance with the ATR requirements. It does not affect whether a loan is a "higher-priced mortgage loan" (HPML) under other Bureau rules and does not exempt a loan from other requirements for HPMLs.

- To calculate whether a loan's APR exceeds the APOR for a comparable loan by more than the relevant 1.5 or 3.5 percentage-point spread, you may use the rate-spread calculators and other guidance available online at http://www.ffiec.gov/ratespread/.

4.4 Are there different types of QMs?

There are four types of QMs. Two types of QMs, the General and Temporary QMs, can be originated by any creditor, regardless of the creditor's size. Two additional types of QMs, Small Creditor and Balloon-Payment QMs, can be originated only by small creditors.

For all four types, QMs that are higher-priced receive a rebuttable presumption and QMs that are not higher-priced receive safe harbor status. However, the definition of "higher-priced" is different for Small Creditor and Balloon-Payment QMs. *(See "What makes a QM loan higher priced?" on page 34.)*

Some requirements are common across all four types of QM. These requirements include:

- A prohibition on negative amortization or interest-only payments
- A prohibition on loan terms in excess of 30 years

- Limitations on points and fees: The threshold is generally 3 percent of the loan balance, but larger amounts are allowed for loans under $100,000 *(See "What are the QM points-and-fees caps and what do I include when calculating points and fees?" on page 43.)*

4.5 What types of QMs can all creditors originate?

There are two types of Qualified Mortgage that all creditors are eligible to originate.

4.5.1 Type 1: General QM definition (§ 1026.43(e)(2))

General QM loans may not have negative-amortization, interest-only, or balloon-payment features or terms that exceed 30 years. They also may **not** have points and fees that exceed the specified limits.

In addition, in order for a loan to be a General QM loan, the creditor must:

- Underwrite based on a fully-amortizing schedule using the maximum rate permitted during the first five years after the date of the first periodic payment
- Consider and verify the consumer's income or assets, current debt obligations, alimony and child-support obligations
- Determine that the consumer's total monthly debt-to-income ratio is no more than 43 percent, using the definitions and other requirements provided in appendix Q, which is derived from the Federal Housing Administration manual

Although consideration and verification of a consumer's credit history is not specifically incorporated into the General QM definition, you must verify a consumer's debt obligations using reasonably reliable third-party records, which may include use of a credit report or records that evidence nontraditional credit references.

When appendix Q does not resolve how a specific type of debt or income should be treated, creditors may rely on guidelines of the GSEs or certain federal agencies (listed below under "Temporary QM definition") to resolve the issue. However, a creditor may not rely on GSE or agency guidelines where such guidelines are in conflict with appendix Q standards.

4.5.2 Type 2: Temporary QM definition (§ 1026.43(e)(4))

The rule also extends QM status to certain loans that are originated during a transitional period if they are eligible for purchase or guarantee by Fannie Mae or Freddie Mac (the government-sponsored enterprises (GSEs)) or for insurance or guarantee by certain federal agencies. Loans that receive QM status under the temporary provision will retain that status after the temporary provision expires, but new loans will not receive QM status after that date under the temporary provision. So, after expiration of the temporary provision, loans must meet the requirements for one of the other categories of Qualified Mortgages to be QMs.

The temporary provision expires, for loans eligible for purchase or guarantee by the GSEs, on the date that the GSEs exit federal conservatorship or receivership or on January 10, 2021, whichever occurs first.

The temporary provision for loans eligible for insurance or guarantee by specified federal agencies is a transition measure designed to give the agencies time to exercise separate authority under the Dodd-Frank Act to determine which of their loans will receive QM status. This temporary provision will expire on the date that the relevant agency's own QM rules take effect or on January 10, 2021, whichever occurs first.

Loans falling under the **Temporary QM definition** must meet the same requirements as General QM loans regarding prohibitions on risky features (negative-amortization, interest-only, and balloon-payment features), a maximum loan term of 30 years, and points-and-fees restrictions.

They must also meet at least **one** of these additional requirements:

- Eligible for purchase or guarantee by the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac) while operating under federal conservatorship or receivership
- Eligible to be guaranteed by the U.S. Department of Agriculture (USDA)
- Eligible to be insured by the Rural Housing Service

Previously, a loan could be a Temporary QM if it was eligible to be guaranteed by the U.S. Department of Veterans Affairs (VA) or was eligible for Federal Housing Administration (FHA) insurance. However, since the initial issuance of the ATR/QM rule, the VA and HUD have issued their own QM rules, and those QM rules have taken effect. Under HUD's and the VA's rules, loans guaranteed, insured, or made by the FHA or the VA are generally QMs.

Eligibility for purchase or guarantee by a GSE or insurance or guarantee by an agency can be established based on the following methods:

- Valid recommendation from a GSE Automated Underwriting System (AUS) or an AUS that relies on an agency underwriting tool
- GSE or agency guidelines contained in official manuals
- Written agreements between a GSE or agency and the creditor (or a direct sponsor or aggregator of the creditor)
- Individual loan waivers from a GSE or agency

To meet the Temporary QM definition, loans must be underwritten using the required guidelines of the entities above, including any relevant DTI guidelines. They do **not** have to meet the 43 percent debt-to-income ratio threshold that applies to General QM loans.

The creditor does not have to satisfy GSE or agency standards which are wholly unrelated to the credit risk or underwriting of the loan or any standards which apply after the consummation of the loan.

4.6 What types of QMs can small creditors originate?

Small creditors can originate Qualified Mortgages under the General and Temporary QM definitions discussed above. In addition, there are two additional types of Qualified Mortgages that can only be originated by small creditors.

You can make these types of QMs only if you meet both of the following requirements:

- You and your affiliates that regularly extended covered transactions (*i.e.*, closed-end residential mortgages that are subject to the ATR requirements) in the last calendar year had assets below $2 billion (to be adjusted annually for inflation by the Bureau) at the end of the last calendar year.

- You and all your affiliates together originated no more than 2,000 first-lien covered transactions in the preceding calendar year. You are not required to count loans that you originated and kept in portfolio or loans that your affiliate originated and kept in its portfolio.

The September 2015 Final Rule created a grace period for creditors that no longer meet the small creditor origination limit or asset-size limit. If you exceeded the asset-size or origination limit during the immediately preceding calendar year but met the limit in the calendar year before the immediately preceding year, you can operate as a small creditor and originate small-creditor QMs for applications you receive before April 1 of the current calendar year.

An affiliate is any company that controls, is controlled by, or is under common control with, your company. This generally means that your affiliates are your parent company, your subsidiaries, and your sister companies. For example, if your organization is a bank owned by a bank holding company that also owns another bank, both the bank holding company and the other bank are your bank's affiliates.

To determine if you meet the asset-size limit, you count your assets and the assets of your affiliates that, during the relevant period, regularly extended first-lien, closed-end mortgages subject to the ATR requirements.

To determine if you meet the originations limit, you count all first-lien, closed-end mortgages subject to the ATR requirements originated by you or one of your affiliates. Do not count subordinate-lien mortgages or mortgages that are not subject to the ATR/QM rule, such as HELOCs, time-share plans, reverse mortgages, or temporary or bridge loans with terms of 12 months or less. *(See "When do I have to start following this rule?" on page 14.)*

4.6.1 Type 1: Small Creditor QM (§ 1026.43(e)(5))

Small Creditor QM loans may not have negative-amortization, interest-only, or balloon-payment features or terms that exceed 30 years. They also may not have points and fees that exceed the specified QM limits. *(See "What are the QM points-and-fees caps and what do I include when calculating points and fees?" on page 43.)*

In addition, in order for a loan to be a Small Creditor QM loan:

- You must underwrite based on a fully-amortizing schedule using the maximum rate permitted during the first five years after the date of the first periodic payment.
- The loan must not be subject to a forward commitment (an agreement made at or prior to consummation of a loan to sell the loan after consummation, other than to a creditor that itself is eligible to make Small Creditor QMs).
- You must consider and verify the consumer's income or assets, and debts, alimony, and child support.
- You must consider the consumer's debt-to-income ratio (DTI) or residual income, although the rule sets no specific threshold for DTI or residual income.

Small Creditor QMs generally lose their QM status if you sell or otherwise transfer them less than three years after consummation. However, a Small Creditor QM keeps its QM status if it meets one of these criteria:

- It is sold more than three years after consummation.
- It is sold to another creditor that meets the criteria regarding number of originations and asset size, at any time.
- It is sold pursuant to a supervisory action or agreement, at any time.
- It is transferred as part of a merger or acquisition of or by the creditor, at any time.

4.6.2 Type 2: Balloon-Payment QM (§ 1026.43 (f))

Small creditors that operate in a rural or underserved area will be able to make Balloon-Payment QMs. Additionally, the September 2015 Final Rule provides a grace period to allow certain creditors that no longer meet these requirements to continue to originate Balloon-Payment QMs for applications received before April 1 of the current year.

For mortgage transactions with applications received on and after March 31, 2016, you can originate Balloon-Payment QMs if you are a small creditor (*i.e.*, you satisfy the asset-size and originations limits), and you operated in a rural or underserved area in the preceding calendar year. If you are not a small creditor or you did not operate in a rural or underserved area in the preceding calendar year, you may be able to originate Balloon-Payment QMs during a grace period. A small creditor that did not operate in a rural or underserved area in the preceding calendar year can originate Balloon-Payment QMs for transactions with applications received prior to April 1 of the current calendar year if the small creditor operated in a rural or underserved area in the calendar year before the preceding calendar year. Similarly, a creditor that operated in a rural or underserved area in the preceding calendar year but that did not satisfy the small creditor origination limit or asset-size limit in the preceding calendar year can originate Balloon-Payment QMs for transactions with applications received before April 1 of the current calendar year if the creditor met the limit in the calendar year before the preceding calendar year.

Balloon-Payment QMs must not have negative-amortization or interest-only features and must comply with the points-and-fees limits for Qualified Mortgages.

In addition:

- The loan must have a fixed interest rate and periodic payments (other than the balloon payment) that would fully amortize the loan over 30 years or less.
- The loan must have a term of five years or longer.
- The loan must not be subject to a forward commitment (an agreement made at or prior to consummation of a loan to sell the loan after consummation, other than to a creditor that itself is eligible to make Balloon-Payment QMs).
- You must determine that the consumer will be able to make the scheduled periodic payments (including mortgage-related obligations) other than the balloon payment. Unlike the calculation of balloon loan monthly payments for determining ATR *(See "Calculating payments under the ATR standard for the loan you are underwriting: § 1026.43(c)(5)" on page 25)*, the Balloon-Payment QM calculation excludes the balloon payment even if the loan is a higher-priced loan,
- You must consider and verify the consumer's income or assets, and debts, alimony, and child support.
- You must consider the consumer's debt-to-income ratio (DTI) or residual income, although the rule sets no specific threshold for DTI or residual income.

Like Small Creditor QMs, Balloon-Payment QMs generally lose their QM status if you sell or otherwise transfer them less than three years after consummation. However, a Balloon-Payment QM keeps its QM status if it meets one of these criteria:

- It is sold more than three years after consummation.
- It is sold to another creditor that meets the criteria regarding operating in rural or underserved areas, number of originations, and asset size, at any time.
- It is sold pursuant to a supervisory action or agreement, at any time.
- It is transferred as part of a merger or acquisition of or by the creditor, at any time.

4.7 Are there special requirements for calculating the DTI ratio on QM loans? (§ 1026.43(e)(2)(vi) and appendix Q)

As described above, the General QM definition requires that a consumer's total debt-to-income ratio not exceed 43 percent. Section 1026.43(e)(2)(vi) and appendix Q of the ATR/QM rule contain the definitions of debt and income for purposes of the General QM definition.

Keep in mind that different DTI rules apply to loans complying under the ATR standard and to the other QM definitions:

- To satisfy the general ATR standard, you must consider DTI or residual income.
- To originate a QM under the temporary definition (eligible for sale to or guarantee by a GSE or insured or guaranteed by a specified federal agency), you must meet the relevant entity's applicable DTI and other requirements.
- To originate a Small Creditor or Balloon-Payment QM, you must consider DTI or residual income, but you do not have to meet a specific threshold requirement.

4.8 What are the QM points-and-fees caps and what do I include when calculating points and fees? (§§ 1026.32(b)(1) and 1026.43(e)(3))

For a loan to be a QM, the points and fees may not exceed the points-and-fees caps. The points-and-fees caps are higher for smaller loans.

- 3 percent of the total loan amount for a loan greater than or equal to $100,000
- $3,000 for a loan greater than or equal to $60,000 but less than $100,000
- 5 percent of the total loan amount for a loan greater than or equal to $20,000 but less than $60,000
- $1,000 for a loan greater than or equal to $12,500 but less than $20,000
- 8 percent of the total loan amount for a loan less than $12,500

The dollar amounts listed above will be adjusted annually for inflation and published each year in the commentary to Regulation Z. *(See § 1026.43(e)(3)(ii) and accompanying Commentary.)*

To determine whether a loan is within the QM points-and-fees caps, follow these steps:

- First, determine which of the caps applies to the loan amount on the face of the note.
- Second, calculate the maximum points and fees for that loan amount:
- For a loan amount that has a **fixed-dollar cap** (for example, $3,000 for loan amounts of $60,000 but less than $100,000), that fixed-dollar cap is the maximum allowable points and fees.
- For a loan amount that has a **percentage cap** (for example, 5 percent of the total loan amount for loan amounts greater than or equal to $20,000 but less than $60,000) determine the “total loan amount” for your transaction. The total loan amount equals the “amount financed” (§ 1026.18) minus any points and fees that are rolled into the loan

amount. Multiply the total loan amount by the percentage cap to determine the maximum allowable points and fees.

- Finally, calculate the total points and fees for your transaction. If the total points and fees for your transaction exceed the maximum allowable points and fees, then the loan is not a QM.

- If, after consummation, you determine that the total points and fees for your transaction exceed the maximum allowable for a QM, the rule allows you to cure that overage if you take certain steps within 210 days after consummation and maintain and follow certain policies and procedures. *See* § 1026.43(e)(3)(iii) and (iv) and the accompanying commentary. (Note that the cure is not available for transactions consummated before the effective date of § 1026.43(e)(3)(iii) and (iv) and when certain events have occurred).

4.8.1 Points-and-fees calculation (§ 1026.32(b)(1))

To calculate points and fees for the QM points-and-fees caps, you will use the same approach that you use for calculating points and fees for closed-end loans under the Home Ownership and Equity Protection Act (HOEPA) thresholds in the Bureau's High-Cost Mortgage and Homeownership Counseling Amendments to the Truth in Lending Act (Regulation Z) and Homeownership Counseling Amendments to the Real Estate Settlement Procedures Act (Regulation X) rulemakings. Those rules are available online at http://www.consumerfinance.gov/regulations/.

Unless specified otherwise, include amounts that are **known at or before consummation**, even if the consumer pays them after consummation by rolling them into the loan amount.

In addition, unless specified otherwise, closing costs that you pay and recoup from the consumer over time through the interest rate are **not** counted in points and fees.

To calculate points and fees, add together the amounts paid in connection with the transaction for the six categories of charges listed below:

1. Finance charge (§ 1026.32(b)(1)(i))

In general, include all items included in the finance charge. (§ 1026.4(a) and (b)). However, you may **exclude** the following types and amounts of charges, even if they normally would be included in the finance charge:

- Interest or the time-price differential
- Mortgage insurance premiums (MIPs)
- Federal or state government-sponsored MIPs: For example, exclude up-front and annual FHA premiums, VA funding fees, and USDA guarantee fees.
- Private mortgage insurance (PMI) premiums: Exclude monthly or annual PMI premiums. You may also exclude up-front PMI premiums if the premium is refundable on a prorated basis and a refund is automatically issued upon loan satisfaction. However, even if the premium is excludable, you must include any portion that exceeds the up-front MIP for FHA loans. Those amounts are published in HUD Mortgagee Letters, which you can access on HUD's website at http://portal.hud.gov/hudportal/HUD?src=/program_offices/administration/hudclips/letters/mortgagee/.
- A charge paid by a third party may be included in points and fees, but is not included in points and fees under § 1026.32(b)(1)(i) if the exclusions to points and fees in § 1026.32(b)(1)(i)(A) through (F) apply. For example, seller's points are not included in points and fees under § 1026.32(b)(1)(i) as they are not included in the finance charge. But they still may be included in points and fees under § 1026.32(b)(1)(ii) through (vi) – for example, if they cover loan originator compensation, credit life insurance premiums, or a prepayment penalty.
- *Bona fide* third-party charges not retained by the creditor, loan originator, or an affiliate of either (§ 1026.32(b)(1)(i)(D))
- In general, you may exclude these types of charges even if they would be included in the finance charge. For example, you may exclude a *bona fide* charge imposed by a third-party settlement agent (for example, an attorney) so long as neither the creditor nor the loan originator (or their affiliates) retains a portion of the charge.

- However, you must still **include** any third-party charges that are specifically required to be included under other provisions of the points-and-fees calculation (for example, certain PMI premiums, certain real estate-related charges, and premiums for certain credit insurance and debt cancellation or suspension coverage). Note that up-front fees you charge consumers to recover the costs of loan-level price adjustments imposed by secondary market purchasers of loans, including the GSEs, are not considered *bona fide* third-party charges and must be included in points and fees.

- *Bona fide* discount points (§ 1026.32(b)(1)(i)(E), 32(b)(1)(i)(F), and 32(b)(3))

- Exclude up to 2 *bona fide* discount points **if** the interest rate before the discount does not exceed the APOR for a comparable transaction by more than 1 percentage point; or

- Exclude up to 1 *bona fide* discount point **if** the interest rate before the discount does not exceed the APOR for a comparable transaction by more than 2 percentage points.

Note that a discount point is "bona fide" if it reduces the consumer's interest rate by an amount that reflects established industry practices, such as secondary mortgage market norms. An example is the pricing in the to-be-announced market for mortgage-backed securities.

2. Loan originator compensation (§ 1026.32(b)(1)(ii))

Include compensation paid directly or indirectly by a consumer or creditor to a loan originator other than compensation paid by a mortgage broker, creditor, or retailer of manufactured homes to an employee. Include compensation that is attributable to the transaction, to the extent that such compensation is known as of the date the interest rate for the transaction is set. In general, include the following:

Compensation paid directly by a consumer to a mortgage broker: Include the amount the consumer pays directly to the mortgage broker. If this payment is already included in points and fees because it is included in the finance charge under § 1026.32(b)(1)(i), it does not have to be included again as loan originator compensation under § 1026.32(b)(1)(ii).

In the context of determining what loan originator compensation must be included in points and fees, the term "mortgage broker" refers to both brokerage firms and individual brokers. Compensation paid by a mortgage broker to an employee is not included in points and fees.

Compensation paid by a creditor to a mortgage broker: Include the amount the creditor pays to the broker for the transaction. Include this amount even if the creditor included origination or other charges paid by the consumer to the creditor as points and fees under § 1026.32(b)(1)(i) as a finance charge or if the creditor does not receive an up-front payment from the consumer to cover the broker's fee but rather recoups the fee from the consumer through the interest rate over time.

Compensation paid by a consumer or creditor to a manufactured home retailer: Include the amount paid by a consumer or creditor to a manufactured home retailer that qualifies as a loan originator under § 1026.36(a)(1) for loan origination activities. Compensation paid by the manufactured home retailer to its employees does not have to be included. § 1026.32(b)(1)(ii)(D) and comment 32 (b)(1)(ii)-5.

Compensation included in the sales price of a manufactured home: Include loan originator compensation that the creditor has knowledge is included in the sales price of a manufactured home. The creditor is not required to investigate the sales price of a manufactured home to determine if the sales price includes loan originator compensation. Comment 32(b)(1)(ii)-5.

3. Real estate-related fees (§ 1026.32(b)(1)(iii))

The following categories of charges are **excluded** from points and fees **only if:**

1. The charge is reasonable;
2. The creditor receives no direct or indirect compensation in connection with the charge; and
3. The charge is not paid to an affiliate of the creditor.

If one or more of those three conditions is **not** satisfied, **you must include** these charges in points and fees even if they would be excluded from the finance charge:

- Fees for title examination, abstract of title, title insurance, property survey, and similar purposes
- Fees for preparing loan-related documents, such as deeds, mortgages, and reconveyance or settlement documents

- Notary and credit-report fees
- Property appraisal fees or inspection fees to assess the value or condition of the property if the service is performed prior to consummation, including fees related to pest-infestation or flood-hazard determinations
- Amounts paid into escrow or trustee accounts that are not otherwise included in the finance charge (except amounts held for future payment of taxes)

4. Premiums for credit insurance; credit property insurance; other life,accident, health or loss-of-income insurance where the creditor is beneficiary; or debt cancellation or suspension coverage payments (§ 1026.32(b)(1)(iv))

Include premiums for these types of insurance that are payable at or before consummation even if such premiums are rolled into the loan amount, if permitted by law.

You do not need to include these charges if they are paid after consummation (*e.g.*, monthly premiums).

Note that credit property insurance means insurance that protects the creditor's interest in the property. It does not include homeowner's insurance that protects the consumer.

You do not need to include premiums for life, accident, health, or loss-of-income insurance if the consumer (or another person designated by the consumer) is the sole beneficiary of the insurance.

5. Maximum prepayment penalty (§ 1026.32(b)(1)(v))

Include the maximum prepayment penalty that a consumer could be charged for prepaying the loan. *(See "Can I charge prepayment fees on a covered transaction?" on page 49 to determine if you are permitted to charge a prepayment penalty).*

6. Prepayment penalty paid in a refinance (§ 1026.32(b)(1)(vi))

If you are refinancing a loan that you or your affiliate currently holds or is currently servicing, then include any penalties you charge consumers for prepaying their previous loans.

7. Charges paid by third parties. (Comment 32(b)(1)-2))

Include charges paid by third parties that fall within the definition of points and fees in § 1026.32(b)(1)(i) through (vi) (discussed above), including charges included in the finance charge. Charges paid by third parties that fall within the exclusions to points and fees in § 1026.32(b)(1)(i)(A) through (F) do not have to be included in points and fees. Seller's points are excluded from the finance charge (see § 1026.4(c)(5)) and therefore can be excluded from points and fees, but charges paid by the seller should be included if they are for items listed as points and fees in § 1026.32(b)(1)(ii) through (vi).

8. Creditor-paid charges. (Comment 32(b)(1)-2))

Charges paid by the creditor, other than loan originator compensation paid by the creditor that is required to be included in points and fees under § 1026.32(b)(1)(ii), can be excluded from points and fees.

4.9 Can I charge prepayment fees on a covered transaction? (§ 1026.43(g))

If you wish to include a prepayment penalty option, you may only do so for fixed-rate or step-rate QMs that are not higher-priced and only when applicable law otherwise permits the prepayment penalty.

Note that the definition of prepayment penalty does not include certain *bona fide* third-party charges that were waived at consummation (and expected to be reimbursed via the interest rate) in cases where the consumer fully prepays the loan within three years and must repay the charges.

Include the maximum prepayment penalty amount when you calculate the loan's fees and points to determine whether the points and fees exceed the limits discussed above. *(See "What are the QM points-and-fees caps and what do I include when calculating points and fees?" on page 45.)*

You cannot impose a prepayment penalty after the first three years of the loan term

A prepayment penalty also **cannot** be greater than:

- 2 percent of the outstanding loan balance prepaid during the first two years of the loan
- 1 percent of the outstanding loan balance prepaid during the third year of the loan

If you wish to charge a prepayment fee, **you must also offer the consumer an alternative transaction that you believe the consumer will qualify for. The alternative loan cannot have** a prepayment penalty. The alternative loan must be similar to the loan with the prepayment penalty, so the consumer can choose between two products he will likely qualify for.

The **alternative loan**:

- Must be a fixed-rate or graduated-payment loan and must match the rate type from the loan with the prepayment penalty
- Must have the same term as the mortgage with the prepayment penalty
- Cannot have deferred principal, balloon or interest-only payments, or negative amortization

When your organization is a broker or table-funds loans and you want to use the safe harbor for compliance with anti-steering rules for loan originators under § 1026.36(e) of Regulation Z, you must show the consumer:

- The loan with the lowest interest rate overall
- The loan with the lowest interest rate with a prepayment penalty
- The loan with the lowest total origination points or fee and discount points

The alternative loans do not have to come from the same secondary market partner. You may show the consumer alternative loans from more than one investor or aggregator.

5. Refinancing from Non-Standard to Standard Loans: ATR Special Circumstance (§1026.43(d))

5.1 Do the standard ATR requirements apply when I refinance consumers from a non-standard to a standard loan? (§ 1026.43(d)(1)(ii)(A))

Many consumers have adjustable-rate, interest-only, or negative-amortization loans that they may not be able to afford when the loan recasts. To give you more flexibility to help these homeowners refinance, the ATR/QM rule gives you the option to **refinance your current mortgage customers** from a **non-standard** mortgage (which includes various types of mortgages that can lead to payment shock and can result in default) into a **standard mortgage** without having to meet the rule's ATR requirements including considering the eight underwriting factors required for ATR.

This option applies only to mortgages your organization holds or services. Subservicers and third parties cannot use it.

You can use this option **only** when:

- The payments under the refinance will not cause the consumer's principal balance to increase.
- The consumer uses the proceeds to pay off the original mortgage and for closing or settlement charges appearing on the HUD-1 settlement statement. The consumer takes out no cash.
- The consumer's monthly payment will materially decrease (*i.e.*, at least 10 percent).
- The consumer has only one 30-day late payment in the past 12 months and no late payments within six months.
- The consumer's written application for the standard mortgage is received no later than two months after the non-standard mortgage has recast.
- You have considered whether the standard mortgage likely will prevent the consumer from defaulting on the non-standard mortgage once the loan is recast.
- If the non-standard mortgage was consummated on or after January 10, 2014, the non-standard mortgage was made in accordance with the rule's Ability-to-Repay requirements or Qualified Mortgage provisions, as applicable.

The new loan has to meet these guidelines:

- The loan cannot have deferred principal, negative amortization, or balloon payments.
- Points and fees must fall within the thresholds for Qualified Mortgages.
- The loan term cannot exceed 40 years.
- The interest rate must be fixed for at least the first five years of the loan.

The ATR/QM rule does not apply when you alter an existing loan without refinancing it. So you can provide a loan modification to a defaulted (or non-defaulted) consumer without complying with ATR. You can find a discussion of what changes to a loan will be treated as a modification rather than a refinancing in Regulation Z at § 1026.20(a).

5.2 How do I calculate non-standard and standard payment amounts to determine whether the consumer's monthly payment on the standard mortgage will represent a material decrease? (§ 1026.43(d)(5))

To calculate payments when comparing non-standard loans to standard loans, first calculate the payment the consumer will have to make if the non-standard loan reaches a **recast** point. **Recast** occurs when:

- For an adjustable-rate mortgage, the introductory fixed-rate period ends.
- For an interest-only loan, the interest-only period ends.
- For a negatively-amortizing loan, the negatively-amortizing payment period ends.

Then calculate the payment for the standard loan, using the fully-indexed rate and the monthly payment that will fully amortize the loan based on equal monthly payments.

Finally, compare the two payments. A material decrease must be evaluated in light of the facts and circumstances for the particular loan. A payment reduction of 10 percent or more meets the "materially lower" standard.

Note that the payment calculation for this special refinancing provision is slightly different from the payment calculation used under the ATR/QM provisions. Under this special provision, you must base the calculation of the maximum loan amount on the amount of principal that will be outstanding at the time of recast, taking into account any principal payments that the consumer will have made by that time.

6. Practical implementation and compliance considerations

You should consult with legal counsel or your compliance officer to understand your obligations under the rule, and to devise the policies and procedures you will need to have in place to comply with the rule's requirements.

How you comply with the rule may depend on your business model. When mapping out your compliance plan, you should consider practical implementation issues in addition to understanding your obligations under the rule. Your compliance plan may include:

1. Identifying affected products, departments, and staff

Creditors may offer some, or all, of the loan products discussed in the ATR/QM rule. To plan for implementation of the rule, you should identify all products, departments, and staff affected by the rule.

2. Identifying the business-process, operational, and technology changes that will be necessary for compliance

The requirements may affect a number of parts of your business systems and processes. The forms and processes you use to communicate internally and externally may be affected by the verification requirements. The systems and processes you use to underwrite loans may also be affected. Secondary marketing and servicing processes and systems may be affected by the special ATR provisions regarding the refinancing of a non-standard loan into a standard loan. It is likely that as you originate new loans after January 10, 2014, you will want to identify those loans on your transaction systems with their definitional status under the rule (*i.e.*, ATR, QM), which may involve creating new data element(s) within your processing systems. Likewise, if the loan is a QM, you probably want to note which level of liability protection the loan is receiving, which may have similar impacts.

Fully understanding the changes required may involve a review of your existing business processes, as well as the hardware and software that you, your agents, or other business partners use. Gap analyses may be a helpful output of such a review and help you to create a robust implementation plan.

3. Identifying critical impacts on key service providers or business partners

Third-party updates may be necessary to obtain required information or verifications; update disclosures, underwriting software, compliance and quality-control systems and processes; and update records-management protocols.

Software providers, or other vendors and business partners, may offer compliance solutions that can assist with any necessary changes. Identifying these key partners will depend on your business model. For example, banks and credit unions may find it helpful to talk to their correspondent banks, secondary market partners, and technology vendors. In some cases, you may need to negotiate revised or new contracts with these parties, or seek a different set of services.

If you seek the assistance of vendors or business partners, make sure you understand the extent of the assistance that they provide. For example, if vendors provide software that calculates loan cost to determine which transactions are higher-priced, do they guarantee the accuracy of their conclusions?

The CFPB expects supervised banks and nonbanks to have an effective process for managing the risks of service provider relationships. For more information on this, view CFPB Bulletin 2012-03 Service Providers.

4. Identifying training needs

Consider what training will be necessary for your loan officers; secondary marketing, processing, compliance, and-quality control staff; as well as anyone else who approves, processes, or monitors credit transactions. Training may also be necessary for other individuals who are your employees, or for the employees of your agents and business partners.

5. Considering other Title XIV rules

The ATR/QM rule is just one component of the Bureau's Dodd-Frank Act Title XIV rulemakings.

Other Title XIV rules include:

- 2013 HOEPA Rule
- ECOA Valuations Rule
- TILA Higher-Priced Mortgage Loans Appraisal Rule
- Loan Originator Rule
- RESPA and TILA Mortgage Servicing Rules
- TILA Higher-Priced Mortgage Loans Escrow Rule

Each of these rules affects aspects of the mortgage industry and its regulation. Many of these rules intersect with one or more of the others. Therefore, the compliance considerations for these rules may overlap in your organization. You will find copies of these rules online at http://www.consumerfinance.gov/regulations/.

7. Other resources

7.1 Where can I find a copy of the ATR/QM rule and get more information about it?

You will find the January 2013 Final Rule on the Bureau's website at http://www.consumerfinance.gov/regulatory-implementation/.

In addition to a complete copy of the January 2013 Final Rule, that web page also contains:

a. The preamble, which explains why the Bureau issued the rule; the legal authority and reasoning behind the rule; responses to comments; and analysis of the benefits, costs, and impacts of the rule

b. Official Interpretations of the rule

c. Links to final rule amendments, including the June 2013 ATR/QM Concurrent Final Rule, the July 2013 Final Rule, the October 2013 Final Rule, the September 2015 Final Rule, and the March 2016 Interim Final Rule.

d. Other implementation support materials including videos, reference charts, and proposed rule amendments

Useful resources related to regulatory implementation are also available at http://www.consumerfinance.gov/regulatory-implementation/.

For email updates about Bureau regulations and when additional implementation resources become available, please submit your email address within the "Email updates about mortgage rule implementation" box at http://www.consumerfinance.gov/regulatory-implementation/.