Wednesday, June 6, 2012

CFPB: Re-Opening "Ability-to-Repay"

On June 5, 2012, the Consumer Financial Protection Bureau (Bureau) announced that it is "reopening the comment period" for the proposed rule, issued on May 11, 2011 by the Federal Reserve Board (Board), addressing the new ability-to-repay requirements that generally will apply to consumer credit transactions secured by a dwelling and the definition of a "qualified mortgage."

The ability-to-repay requirements were set forth in the May 11, 2011 proposal to amend Regulation Z (the implementing regulation of the Truth in Lending Act (TILA) to implement amendments to TILA made by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank).

Since then, pursuant to Dodd-Frank, the Board's rulemaking authority for TILA was transferred to the Bureau as of July 21, 2011. The original comment period to the proposed rule closed on July 22, 2011.

The Bureau is reopening the comment period until July 9, 2012 to seek comment specifically on certain new data and information submitted during or obtained after the close of the original comment period.

I have written extensively about the ability-to-repay. And I would urge you to read some of these articles to become familiar with these important requirements:*

Ability-to-Repay: Regulating or Underwriting? Part I
Ability-to-Repay: Regulating or Underwriting? Part II
Ability-to-Repay: The Basics and a Chart
Ability-to-Repay: The Chart
Ability-to-Repay: Additional Analysis
FRB: Proposes Rule - Ability-to-Repay

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History

Sections 1411, 1412, and 1414 of the Dodd-Frank created new TILA section 129C, which, among other things, established new ability-to-pay requirements. If a mortgage is a so-called "qualified mortgage," the compliance with the ability-to-repay rule would offer a presumption of compliance.

The word 'presumption' is a dispositive word in this proposal. Please keep the phrase "presumption of compliance" in mind as you read through this brief outline.

On May 11, 2011, the Board published for notice and comment a proposed ability-to-repay rule, amending Regulation Z to implement new TILA section 129C. The comment period for this initial proposal closed on July 22, 2011.

Then, on July 21, 2011 Dodd-Frank transferred the Board's rulemaking authority for TILA, among other consumer financial protection laws, to the Bureau. Accordingly, all comment letters on the proposed rule were also transferred to the Bureau. According to the Bureau, in response to the proposed rule approximately 1800 comment letters were received from numerous commenters, including members of Congress, lenders, consumer groups, trade associations, mortgage and real estate market participants, and individual consumers.

Even after the comment period closed, various interested parties, including industry and consumer group commenters, submitted to the Bureau oral and written *ex parte* presentations on the proposed rule.

Through various comment letters, *ex parte* communications, and the Bureau's own collection of data, the Bureau has received additional information and new data pertaining to the proposed rule.

The Bureau is now interested in providing opportunity for additional public comment on these materials. Thus, it is reopening the comment period until July 9, 2012, in order to request comments specifically on certain additional information or new data, but not other aspects of the proposed rule already submitted previously.

So, what are the new data?

New Data

The Bureau now seeks comment on mortgage loan data that the Bureau has received from the Federal Housing Finance Agency (FHFA). To date, the Bureau has received a sample drawn from the FHFA's Historical Loan Performance (HLP) data along with tabulations from the entire file.

The data include a one percent random sample of all mortgage loans in the HLP data from 1997 through 2011. Tabulations of the HLP data by the FHFA show the number of loans and performance of those loans by year and debt-to-income (DTI) range.

The HLP data consists of all mortgage loans purchased or guaranteed by the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (jointly, the GSEs), but does not include loans backing private-label mortgage-backed securities (MBS) bought by the GSEs.

The data contains loan-level information on characteristics and performance of all single-family mortgages purchased or guaranteed by the GSEs. FHFA updates the HLP data quarterly with information from each GSE.

Among other elements, the data includes product type; payment-to-income and debt-to-income (PTI/DTI) ratios at origination; initial loan-to-value (LTV) ratios based on the purchase price or appraised property value and the first-lien balance; and credit scores.

The Bureau proposes to use these data to tabulate volumes and performance of loans with varying characteristics and to perform other statistical analyses that may assist the Bureau in defining loans with characteristics that make it appropriate to presume that the lender complied with the ability-to-pay requirements or assist the Bureau in assessing the benefits and costs to consumers, including access to credit, and covered persons of, as well as the market share covered by, alternative definitions of a "qualified mortgage."

For example, the Bureau is going to examine various measures of delinquency and their relationship to other variables, such as a consumer's total DTI ratio. Specifically, the Bureau obviously believes that loan performance, as measured by delinquency rate such as 60 days or more delinquent, is an appropriate metric to evaluate whether consumers had the ability to repay those loans at the time made.

Excluding loans for investor-owned properties, low-or no-document mortgages, interest-only (IO) mortgages, negatively-amortizing mortgages (such as payment option-ARMs), or mortgages with a balloon payment feature, the Bureau notes that specific tabulations include first-lien mortgages for first or second homes, that have fully documented income and that are fully amortizing with a maturity that does not exceed 30 years.

Questions and Comments

The following six (6) questions are posed by the Bureau to elicit comments.

1. The Bureau seeks comment on the data received from the FHFA and commercially available data on mortgages securitized into private label securities, including the data source, parameters, and whether other data or studies are available or more appropriate for the purposes indicated above.

2. The Bureau requests data or tabulations for loans not covered in the FHFA data, including loans insured by the Federal Housing Administration (FHA loans), the Department of Veterans Affairs (VA loans), the Department of Agriculture and the Rural Housing Service (RHS loans); or loans held in portfolio or securitized outside of the GSEs or a federal agency, which would be appropriate for the purposes indicated above.

3. The Bureau seeks comment and data on any measures of loan performance and their relationship to a consumer's DTI ratio.

4. The Bureau seeks comment and data on any measures of residual income, the use of such measures in loan underwriting, the relationship of these measures to loan performance, and their relationship to measures of consumer expenditures.

5. The Bureau seeks comment and data regarding any measures of the amount of liquid financial reserves available to meet (i) mortgage-related obligations or (ii) current obligations, the use of such measures in loan underwriting, and the relationship of these measures to loan performance.

6. The Bureau seeks comment and data regarding any measures of stable income and timely housing payments, the use of such measures in loan underwriting, and the relationship of these measures to loan performance.

Litigation and Liability

The Bureau is seeking comment and data on estimates of litigation costs and liability risks associated with claims alleging a violation of ability-to-repay requirements for a mortgage

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loan that is not a "qualified mortgage," in addition to costs and risks that might apply to a "qualified mortgage."

Dodd-Frank Act creates special remedies for violations of TILA section 129C(a) and provides that the statute of limitations for an action for a violation of TILA section 129C is three years from the date of the occurrence of the violation. In addition, Dodd-Frank provides that a consumer may assert a violation of TILA section 129C as a defense to foreclosure by recoupment or set off without regard for the time limit on a private action for damages.

However, new TILA section 129C, among other things, provides a presumption of compliance with the ability-to-repay requirements if the mortgage loan is a "qualified mortgage." In order to implement this special protection from liability, the Board proposed two alternative definitions of a "qualified mortgage" that would provide either a legal safe harbor or a rebuttable presumption that the ability-to-repay requirements had been met.

The Bureau is reopening the comment period to seek comment and data on various factors the Bureau believes are relevant to analyzing estimated costs associated with litigation for a claim alleging a violation of ability-to-repay requirements.

Foreclosure

An area of particular interest is foreclosure. Dodd-Frank provides that a borrower may assert a violation of the ability-to-repay requirements as a defense to foreclosure.

Therefore, the Bureau believes that estimates of serious delinquency and number of homes entering foreclosure are critical to measuring the potential costs of ability-to-repay litigation risk. Although aggregate data on serious delinquency and homes entering foreclosure are available from various sources such as the Mortgage Bankers Association National Delinquency Survey, the Bureau has noted that more granular estimates of homes entering foreclosure can be estimated from the FHFA data and other data sources.

So, the Bureau seeks comments on:

1.The most appropriate measure of delinquency for purposes of calculating potential costs associated with ability-to-repay litigation in the foreclosure context; and,

2. Estimates of potential lawsuits asserting an ability-to-repay violation during the first three years after consummation - when the borrower has not yet defaulted but nevertheless sues the lender.

Litigants and Complaints

Consumer groups have argued that due to the complexity of mortgage-related litigation, such as a violation of TILA, asserting an ability-to-repay violation would require access to a lawyer. These groups noted that appropriate proxies for the number of complaints filed would be the percentage of borrowers in foreclosure who are represented by a lawyer as well as the number of other types of TILA violation cases.

The Bureau notes that survey and other data indicate that a majority of borrowers in default would not have legal representation.

Therefore, the Bureau seeks comments on:

Whether and if so, how the number of lawsuits alleging an ability-to-repay violation would vary under the following circumstances:

(a) The mortgage loan is conceded not to be a "qualified mortgage."

(b) The mortgage loan is claimed to be a "qualified mortgage."

Outcomes from Litigation

As I noted above, Dodd-Frank provides special statutory remedies for violations of TILA section 129C(a), which, for the record, can include an award of damages in the amount equal to the sum of all finance charges and fees paid by the consumer within the three-year statute of limitations and in the case of a defense to foreclosure, recoupment or set off.

In consideration of the outcome from litigation and damages, the Bureau seeks comments on:

1. The likelihood of potential outcomes of litigation, such as dismissal, summary judgment, settlement, or judgment after trial, and the effect on costs under various scenarios including:

(a) The mortgage loan is conceded not to be a "qualified mortgage."

(b) The mortgage loan is claimed to be a "qualified mortgage."

2. Assumptions about a loan, such as interest rate, purchase price, finance charges, and fees, required to calculate average amount of damages awarded in a TILA case involving a violation of the ability-to-repay requirements.

3. The impact of other aspects of damages, such as a consumer's attorney's fees, and lender's litigation costs.

Factors or Costs

Two other areas of interest are being considered by the Bureau, subsumed as "factors" or "costs."

Thus, the Bureau seeks comments on:

1. Whether any additional factors should be considered in assessing the litigation-related costs associated with the ability-to-repay requirements.

2. Any other potential costs of ability-to-repay litigation, including:

(a) Costs associated with risks that loans are "put back" to originators by secondary market participants due to a potential ability-to-repay claim or proven violation. Factors that may determine the total cost of put backs may include: (i) Number and type of representation and warranty provisions in purchase and sale agreements going forward; (ii) number of loans that could potentially be put back; (iii) frequency of put backs being realized; and (iv) cost to lender net of any recovery through foreclosure or sale.

(b) Costs associated with extended foreclosure timelines due to ability-to-repay litigation.

Library

Consumer Financial Protection Bureau

Notice of Reopening of Comment Period
and Request for Comment.
Truth in Lending (Regulation Z)

Federal Register
June 5, 2012

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Labels: Ability to Repay, CFPB, Consumer Financial Protection Bureau, Dodd-Frank Act, Foreclosure, Qualified Mortgage, Qualified Residential Mortgage, Regulation Z, TILA, Truth in Lending Act

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