Comments

of the

National Consumer Law Center (on behalf of its low-income clients)

Consumer Federation of America

and

Prosperity Now

on

Qualified Mortgage Definition under the Truth-in-Lending Act (Regulation Z):

General QM Loan Definition

85 Fed. Reg. 41716

RIN 3170-AA98

Docket No. CFPB-2020-0020

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I. Introduction

Thank you for the opportunity to comment on the Consumer Financial Protection Bureau's ("Bureau") proposed rule, Qualified Mortgage Definition under the Truth in Lending Act (Regulation Z): General QM Loan Definition. The National Consumer Law Center[1] (on behalf of its low-income clients), Consumer Federation of America (CFA),[2] and Prosperity Now[3] submit these comments based on the experiences of our organizations as well as developments that advocates and housing counselors in the field have reported to us.

We strongly urge the Bureau to reconsider its price-based approach to Qualified Mortgages (QM). The Bureau's proposal is not a measure of an individual borrower's ability to repay (ATR) as required under the Truth in Lending Act (TILA). The Bureau has failed to adequately consider reasonable alternatives to its proposal, including: extending the GSE patch while conducting research to determine a more holistic measurement of ATR than debt-to-income (DTI); a compensating factors approach modeled on existing underwriting requirements; or a hybrid price and DTI approach. The Bureau's proposal, if finalized as proposed, assumes loans will be affordable based on early, market-wide defaults rates, an approach that will leave many vulnerable homeowners with unaffordable loans and little recourse. This pricing model also incorporates existing racial disparities in loan pricing and exacerbates the negative impacts of both market expansions and contractions. The Bureau's proposal does not satisfy its obligation to ensure that homeowners can obtain mortgage market access that is affordable and responsible.

In evaluating any proposal, the Bureau is bound by the Dodd-Frank Act's mortgage origination mandate: that "consumers are offered and receive residential mortgage loans on terms that reasonably reflect their ability to repay."[4] Consistent with its general mandate to "ensur[e] that responsible, affordable mortgage credit remains available,"[5] the Bureau is permitted to adjust the statutory QM criteria upon a finding that such adjustments "are necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers."[6] Any adjustments to the QM definition done by the Bureau must therefore rely on

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[1] Since 1969, the nonprofit National Consumer Law Center® (NCLC®) has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitative practices, help financially stressed families build and retain wealth, and advance economic fairness. These comments were written by Steve Sharpe, Alys Cohen and Andrew Pizor, NCLC staff attorneys. For further discussion, please contact Steve Sharpe at ssharpe@nclc.org.

[2] Consumer Federation of America (CFA) is a nonprofit association of some 300 national, state, and local pro-consumer organizations created in 1968 to represent the consumer interest through research, advocacy, and education. Mitria Wilson-Spotser and Barry Zigas worked on these comments for CFA.

[3] Prosperity Now believes that "prosperity" starts with financial security—which means not being one paycheck away from financial disaster, and having savings to obtain assets that build wealth, like a house or an education. Additionally, we assert that the backbone to financial security is financial mobility – the opportunity to climb the economic ladder for a brighter future. Doug Ryan worked on these comments for Prosperity Now.

[4] 15 U.S.C. § 1639b(a)(2) (stating the purpose of 15 U.S.C. §§ 1639b, 1639c).

[5] 15 U.S.C. § 1639b(a)(1).

[6] 15 U.S.C. § 1639c(b)(3)(B)(i).

an adequate demonstration that the credit extended to borrowers under the adjusted definition is both responsible and affordable.

The proposed pricing model is built on market-wide default rates and does not ensure that any particular individual has the ability to repay a loan. The Bureau bases its conclusion that pricing is an adequate proxy for ATR on early default rates. Early defaults on individual loans may demonstrate a lack of ATR, but the converse is not true. Many housing counselors and legal services lawyers have had clients who went without food or medicine or utilities in order to make mortgage payments. Moreover, historical early default rates across the market are distinct from an individual borrower's circumstances and ATR. They, therefore, are not an adequate basis for an irrebuttable presumption that a creditor made a reasonable and good faith determination of a borrower's ability to repay a mortgage loan.[7]

The impact of unaffordable lending does not fall on all communities equally. The last great wave of irresponsible, unaffordable lending stripped communities of color—particularly Black communities—of more than a generation of wealth.[8] Those of us who have represented individual clients remember clients whose lives were destroyed by unaffordable loans, including loans that would meet the safe harbor test the Bureau is proposing. Keying the ATR requirement primarily to price, even with product restrictions, assumes that pricing is rational. Yet, a system geared to portfolio performance and credit risk dispersed across many market players resulted in widespread abusive practices just over a decade ago.

We note that this rulemaking comes during a national health and economic crisis of unprecedented proportions, coupled with a long overdue racial reckoning. Given the fragility of the market and the extreme vulnerability of many consumers at the present moment, the Bureau should proceed with caution and preserve the QM patch. Full engagement by all stakeholders is not possible now. Resources are significantly strained in responding to the pandemic, its economic fallout, and the disproportionate impact both are having on communities of color. We do not yet know how long this crisis will last and how severe it will be. Prudence would counsel that QM must wait, as would a commitment to full engagement with all stakeholders.

We would also ask the Bureau to defer this rulemaking until it can complete the needed research. When the Bureau finalized the 2013 QM rule, it acknowledged that residual income can be a better measure of ATR than DTI. It acknowledged that it would study residual income as part of the five-year assessment.[9] To our knowledge the Bureau still has not conducted any meaningful research into residual income or any other alternative measures of ATR. The Bureau has alternatives to its current proposal and should take the time to develop a proposal that ensures affordable and responsible lending rather than reverting to a level of consumer protection and market regulation that shields predictably unaffordable lending from meaningful consequences.

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[7] 15 U.S.C. § 1639c(a)(1) ("no creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination . . . that . . . the consumer has a reasonable ability to repay the loan.").

[8] *See, e.g.,* Dedrick Asante-Muhammad, Chuck Collins, Josh Hoxie, & Emanuel Nieves, Prosperity Now, *The Road to Zero Wealth: How the Racial Wealth Divide Is Hollowing Out the Middle Class* 8 (Sept. 2017), https://prosperitynow.org/sites/default/files/PDFs/road_to_zero_wealth.pdf (showing decline in both African-American and Latino household wealth over the period from 2007-2013 to levels below household wealth thirty years earlier).

[9] 85 Fed. Reg. 41716, 41728.

As we discussed at length in our comments to the advanced notice of proposed rulemaking (ANPRM),[10] the Bureau's obligation to ensure access to affordable, responsible mortgage credit is tied to the Bureau's obligation to address fair lending. The Bureau's proposal seeks to include historically underserved borrowers, yet the Bureau has not used its central tools to oversee fair lending in the markets. In the nearly three years since Director Cordray left the CFPB, the Bureau has brought one fair lending discrimination case.[11] We continue to urge the Bureau to use all of the tools at its disposal to increase the access to responsible, affordable mortgage loans across all of our communities. The Bureau's singular focus on deregulation to achieve increased access, without meaningfully engaging with its fair lending duties, falls short of its statutory obligations.

II. Recommendations

- Fundamentally, the Bureau would best fulfill its statutory obligations by abandoning the pricing approach, restarting the necessary foundational research to determine how best to ensure affordable and responsible mortgage credit, and, in the interim, extending the GSE patch because 1) it would maintain the overall use of a multi-factor underwriting approach that takes into consideration compensating factors and 2) would involve little hardship on creditors since the vast majority of mortgage loans today are being underwritten and financed through either the GSEs or FHA, which uses its own QM definition and a multi-factor underwriting approach.
- If the Bureau insists on proceeding with a QM rule that allows the patch to expire without further research, a hybrid approach that incorporates both DTI and price better meets the statutory goal and conforms to available data than either the current proposal or a pure DTI-based approach.
- We recommend that the Bureau expand the General QM definition to include loans with a DTI ratio of up to 45%, using the current dividing line between safe harbor and rebuttable presumption QMs.
- We further recommend that the Bureau consider expanding the rebuttable presumption QM boundary to include loans with a higher DTI and low pricing. For example, based upon the data set forth in the Bureau's proposal, the Bureau could consider treating loans with a DTI

[10] Comments of the Atlanta Legal Aid Society, Inc., Consumer Federation of America, National Consumer Law Center (on behalf of its low-income clients), the National Association of Consumer Advocates, and the National Community Stabilization Trust on Qualified Mortgage Definition under the Truth in Lending Act (Regulation Z) 84 Fed. Reg. 37155, Docket No. CFPB–2019–039 (September 16, 2019), https://www.nclc.org/images/pdf/foreclosure_mortgage/dodd-frank/comments-to-cfpb-qualified-mortgage-sept2019.pdf.

[11] Complaint, Bureau of Consumer Financial Protection v. Townstone Financial, Inc. 1:20-cv-04176 (July 15, 2020); *cf.* Kate Berry, *Where have all the CFPB fair-lending cases gone?*, Am Banker (Dec. 16, 2019), https://www.americanbanker.com/news/where-have-all-the-cfpb-fair-lending-cases-gone (noting CFPB referred no cases to the U.S. Department of Justice for ECOA in 2018; 40 cases referred during 2012-2017, or an average of nearly 7 cases/year); Bureau of Consumer Fin. Prot., *Fair Lending Report of the Bureau of Consumer Financial Protection, April 2020*, 85 Fed. Reg. 27395 (May 8, 2020) (CFPB referred three ECOA discrimination cases to US DOJ during 2019, or less than half as many as the average under Director Cordray).

up to 48% and a price at or below the average prime offer rate (APOR) plus 100 basis points as rebuttable presumption QM loans.

- In addition, if the Bureau finalizes a QM definition that relies primarily on pricing to determine safe harbor status, the Bureau should:
    - Maintain the levels for the safe harbor and the rebuttable presumption as proposed without any emergency exceptions, as the risks of default increase with the pricing threshold;
    - Align the pricing thresholds for small dollar mortgage loans with other loans;
    - Clarify that a pricing safe harbor cannot be used to undermine fair lending;
    - Restate that lending based on the borrower's equity or loan to value (LTV) cannot qualify as a QM;
    - Establish strong rules for "consider" and "verify."
- The Bureau should, under no circumstances, negate the basic goals and remedy scheme of the statute by creating a new "seasoning" QM.

III. Pricing is an inadequate proxy for the statutory requirement of ATR

A. The Dodd-Frank Act requires an individualized determination of a borrower's ATR

1. The question is whether the individual borrower is able to repay, not how the loan or portfolio performs

The Truth-in-Lending Act (TILA) requires creditors to make a reasonable and good faith determination, borrower by borrower, loan by loan, of ability to repay.[12] ATR is part of the purpose of the Dodd-Frank Act mortgage origination provisions.[13] While Congress contemplated that the Bureau could establish presumptions of ability to repay in adjusting the QM definition, or even leave the statutory QM definition unadjusted, it nowhere relieved the Bureau of its obligation to ensure affordable and responsible mortgage lending, which Congress grounded in individual borrowers' ATR.

Congress's first assumption in giving the Bureau authority to adjust the QM definition was that the Bureau would make adjustments based on DTI, with other "alternative measures" of ATR as a backstop:

> [A qualified mortgage includes one] that complies with any guidelines or regulations established by the Bureau relating to ratios of total monthly debt to monthly income or alternative measures of ability to pay regular expenses after payment of total monthly debt, taking into account the income levels of the borrower and such other factors as the Bureau may determine relevant and consistent with the purposes described in paragraph (3)(B)(i).[14]

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[12] 15 U.S.C. § 1639c(a)(1).
[13] 15 U.S.C. § 1639b(a)(1) ("It is the purpose of this section and section 1639c of this title to assure that consumers are offered and receive residential mortgage loans on terms that reasonably reflect their ability to repay the loans . . .").
[14] 15 U.S.C § 1639c(b)(2)(a)(vi).

The Bureau is charged with measuring ATR "taking into account the income levels of the borrower," using measures that reflect the ability not just to repay the mortgage loan but other regular expenses. The Bureau may consider additional factors in adjusting the QM definition, but only after and to the extent it has first gauged whether the adjustments reflect individual borrowers' income, debt, and ability to pay other, non-mortgage expenses.

2. LTV ratios are prohibited as grounds for ATR determination

The statute is clear that "the consumer's equity in the dwelling or real property that secures repayment of the loan" cannot be part of an ATR determination.[15] Congress included this express prohibition because of the long and sordid history of asset-based lending. The financial regulators had all recognized asset-based lending as a per se predatory practice by the time the Dodd-Frank Act was passed,[16] but the Dodd-Frank Act created a federal, statutory prohibition on asset-based lending.

Because of this express ban on including the consumer's equity in an ATR determination, loan-to-value ratios are also not permissible in an ATR determination. Loan-to-value ratios are simply the inverse of the consumer's equity, measured at the time of origination. Thus, LTV ratios are no more a proper measure of ATR under TILA than a creditor's profit margin in originating a loan, regardless of how relevant both are to determining the creditor's pricing and risk.

By extension, LTV ratios cannot legally form part of the QM definition. The purpose of the QM definition is to determine whether the lender presumptively has complied with the obligation to assess ATR. The Bureau cannot create a standard that leads to the consideration of prohibited measures.

3. The Dodd-Frank Act requires ATR, not a price cap

While the statutory QM definition includes certain product restrictions, including limits on adjustable rate mortgages, prepayment penalties, and negative amortization, the only direct price limitation set by the statute is a limitation on total points and fees to three percent.[17] Congress could have chosen to address the problems it saw with the mortgage market by creating a price cap, and it could have told the Bureau to measure ATR via pricing—but it did not.

The Bureau argues that the 1994 Home Ownership and Equity Protection Act (HOEPA), and the Federal Reserve Board's creation of additional protections for higher-priced mortgage loans, somehow "provide[s] support for a price-based approach to the General QM

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[15] 15 U.S.C. § 1639c(a)(3).
[16] *See* 2007 Interagency Statement on Subprime Lending, 72 Fed. Reg. 37569, 37573-574 (July 10, 2007) (loans should be underwritten on ATR, not collateral).
[17] 15 U.S.C. § 1639c(b)((2)(A)(vii).

definition."[18] But Congress did not create a limit on the price of mortgage loans, nor did it tie ATR determinations to price, beyond two limited exceptions: 1) the limit on points and fees mentioned above, and 2) an exception to the general ATR rules, where a federally-insured or - guaranteed loan refinances a higher interest rate loan.[19] Nothing in Congress's construction of the ATR requirement or the QM definition suggests that it believed it was generally appropriate to tie ATR to the price of a loan. Indeed, Congress specifically forbade the Bureau from establishing price caps,[20] suggesting at the very least Congressional disapproval of pricing as the sole method for the Bureau to distinguish categorically between responsible and abusive mortgage lending.

Providing additional protections for loans above a certain pricing threshold, as Congress did in passing HOEPA or the Board did when mandating certain underwriting requirements for higher-priced mortgage loans recognizes that, as loan price increases, so do the risks of abusive lending.[21] But nothing in that history suggests that Congress intended to suggest that loans below a certain price point are responsible and affordable, either *de jure* or *de facto.*

B. Pricing is a flawed substitute for ATR

1. Pricing is based on credit risk, not ATR

a) Credit risk is determined by many non-ATR factors

Although the Bureau asserts that pricing is a "more holistic and flexible measure of a consumer's ability to repay"[22] than DTI, the Bureau makes a fatal error in conflating credit risk, the risk of loss to the lender or investor, with ATR. Pricing is not primarily an assessment as to whether or not an individual borrower, at that moment in time, has the ability to repay the loan. Pricing is primarily an assessment of what the creditor can and must charge the borrower to ensure its desired profitability, after accounting for possible risk of loss.

Nor are pricing decisions necessarily geared to individualized assessments of either the loan or the borrower. While pricing decisions *may* be made individually, after a careful assessment of the risks and rewards of a given loan, in those cases, for responsible lenders, the borrower's ATR is one factor among many in making that determination. But more commonly, pricing decisions are made based on rate sheets or software programs that spit out a number, based on assigning the loan to a certain tier of pricing, factoring in certain characteristics of the loan. In those cases, there is not necessarily any assessment of an individual borrower's ATR, even if factors such as the borrower's income and debt load are fed into the program.

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[18] 85 Fed. Reg. 41716, 41720 (July 10, 2020).

[19] 15 U.S.C. § 1639c(a)(5)(D). Even here, the price regulation is not absolute, as refinancing is permitted on a streamlined basis to a higher-rate loan if the borrower is refinancing out of an adjustable rate mortgage to a fixed rate mortgage.

[20] 12 U.S.C. § 5517(o).

[21] *Cf.* Donald P. Morgan & Michael R. Strain, Federal Reserve Bank of New York Staff Reports, *Payday Holiday: How Households Fare after Payday Credit Bans* 12-13 (Feb. 2008), www.newyorkfed.org/research/staff_reports/sr309.pdf (discussing the economic model for how increased interest rates may push households into default).

[22] 85 Fed. Reg. 41716, 41717.

The main drivers of pricing often include no measure of individual ATR. For example, a cursory review of publicly available rate sheets, establishing loan pricing, shows no individualized consideration of borrowers' income or debts or ability to pay expenses beyond what may be reflected in a credit score, combined loan-to-value ratio, or past bankruptcy.[23] The Bureau's consumer-facing "Explore Interest Rates" web site, built to educate consumers about loan pricing and empower them to be more effective market participants, varies, by state, based on loan amount, credit score, LTV, and loan type.[24] The Bureau mentions other drivers of pricing, including fees, points, mortgage insurance, and closing costs, but nowhere suggests to borrowers that their ability to repay a loan—in terms of their available income or other debts—will impact pricing. If pricing reflects ATR, it must surely do so very indirectly.

The fact that a particular borrower receives a low loan price may reflect merely an assessment that the borrower has so much equity that the risk of loss to the lender is low, a statutorily forbidden basis for the ATR determination.[25] Or a low loan price may reflect judgments on future price appreciation (which may be tied to the neighborhood's racial composition).[26] Racial disparities persist in pricing, with people and communities of color paying more.[27]

Others have made the case that pricing of loans above prime rates is set by secondary market participants, unacquainted with any particularities of a borrower's situation, to compensate secondary market participants for the increased risk of loss created by both securitization and creditors' failure to assess ATR.[28] The secondary market is not pricing for ATR because it is not looking at ATR.[29] As the Bureau observed in its assessment of the 2013 ATR rule, "industry has not developed a common approach to measuring and predicting ATR risk, as it has accomplished for other types of risk, such as prepayment and default."[30] Indeed, it is this very lack of engagement by the secondary market in defining ATR that leads to what the Bureau charitably termed "market anxiety"[31] about the hypothetical litigation risk arising from the original creditor's failure to make a good faith, reasonable determination of that borrower's

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[23] *See* https://www.axosbank.com/-/media/Axos/Documents/rate-sheets/Axos-Bank-Wholesale-Mortgage-Express-Rate-Sheet.pdf (page 1); https://onlineapps.fremontbank.com/Affiliates/Documents/Rates/Wholesale%20Rate%20Sheet.pdf (page 3); https://legacy.unionbank.com/Images/CurrentRateSheet.pdf (page 8).

[24] https://www.consumerfinance.gov/owning-a-home/explore-rates/ (last visited September 8, 2020, 11:45 a.m. ET).

[25] *See* III.A.2, *supra.*

[26] *See* Michela Zonta, Ctr. for Am. Progress, *Racial Disparities in Home Appreciation* (July 15, 2019), https://www.americanprogress.org/issues/economy/reports/2019/07/15/469838/racial-disparities-home-appreciation.

[27] *See* III.D.1, *infra.*

[28] *See, e.g.,* Kathleen C. Engel & Patricia A. McCoy, *Turning a Blind Eye: Wall Street Finance of Predatory Lending*, 75 Fordham L. Rev. 2039, 2057-2060 (2007).

[29] 78 Fed. Reg. 6408, 6513 (Jan. 10, 2013) ("investors . . . view [ATR compliance] as the responsibility of the creditor.").

[30] Bureau of Consumer Fin. Prot., *Ability-to-Repay and Qualified Mortgage Rule Assessment Report* at 118 (Jan. 2019), https://files.consumerfinance.gov/f/documents/cfpb_ability-to-repay-qualified-mortgage_assessment-report.pdf.

[31] 78 Fed. Reg. 6408, 6533. *See also id.* at 6505 (suggesting the "widespread fear" expressed by creditors is largely baseless).

ATR.[32] Because the secondary market does not assess and does not know whether or not there is ATR in any given loan, it cannot size the (negligible at most) litigation risk.[33]

Even to the extent loan pricing is based on perceived default risk and not risk of loss, creditors do not always know how to price for that default risk. Creditors may also offer low loan rates to borrowers they perceive as likely to repay the loan, whether the borrower actually has the ability to repay or not. And, while default rates–particularly early default rates–are correlated with ATR, ATR at the time of loan origination is not the sole or even primary driver of default rates.[34]

Creditors supporting the pricing approach have also argued that their pricing reflects their understanding of a loan's default risk–those with higher credit risks or more uncertain ability to repay will be priced significantly higher, thus rationalizing the price approach. However, the ATR provisions were enacted precisely because the market as a whole failed to appropriately price loan risk in the run up to the financial crisis, helping to support a wave of unsustainable credit that left millions of borrowers and investors in deep financial distress. The same economic factors that drove irresponsible lending in the past such as competition for market share and internal compensation plans that reward volume over loan performance, remain in place today. Restrictions in the Dodd-Frank Act designed to curb lender abuses have reduced the danger from these factors but has not eliminated them.

Long-standing Supreme Court precedent establishes that presumptions must have "an immediate connection with … the established fact from which it is inferred."[35] But there is no basis to conclude that pricing, taken as a whole, has an immediate connection with ATR. Rather, pricing reflects the creditor's holistic, sometimes flawed, assessment of its credit risk. It is not primarily a measure, holistic or not, of the borrower's ability to repay the loan.

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[32] As the Bureau found in its 2013 rule, there is no meaningful litigation risk associated with the ATR rule. *See* 78 Fed. Reg. 6408, 6511 ("[T]he Bureau believes the litigation costs will be small and manageable . . . ."); *id.* at 6513 ("[Litigation] costs . . . will not affect either the pricing of the loans or the availability of a secondary market for these loans."). Although the current Bureau asserts that providing a safe harbor from litigation risk has "potential benefits of greater competition and access to credit," 85 Fed. Reg. at 41716, 41739, it provides no new evidence and no reasoned justification that would support a finding that the litigation risk has any actual impact on either competition or access to credit. Indeed, the proposal on which we submit comments mentions "litigation risk" five times, all in a cursory fashion, three of those times relying on the 2013 Rule's discussion and once on the Assessment's discussion. By comparison, the 2013 Rule mentions "litigation risk" 20 times, including an extended discussion of the evidence concerning litigation risk, spanning two pages and four columns in the Federal Register. 78 Fed. Reg. 6408, 6512-6513.

[33] *See, e.g.,* Bureau of Consumer Fin. Prot., *Ability-to-Repay and Qualified Mortgage Rule Assessment Report*, at 265 (Jan. 2019), https://files.consumerfinance.gov/f/documents/cfpb_ability-to-repay-qualified-mortgage_assessment-report.pdf (reporting that a trade group commented that "*unknown* litigation risks associated with non-qualified mortgages has been a primary factor in the failure of investors to support a reemergence of private label security markets") (emphasis added).

[34] *See* Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 37 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), *available at* https://www.nber.org/papers/w21630 (noting that residual income *at the time of default* is highly correlated with default, but not residual income at the time of origination). *See generally III. . C*III. C, *infra.*

[35] Manning v. John Hancock Mut. Life Ins. Co., 100 U.S. 693, 697-98 (1879). *See also* Home Ins. Co. v. Weide, 78 U.S. 438, 441–42(1870) ("A presumption is an inference as to the existence of a fact not actually known, arising from its usual connection with another which is known . . .").

b) Creditors' reliance on LTV in pricing does not reflect ATR

In pricing loans, creditors—whose ultimate concern is with respect to their potential profits and losses and not the impact of the loans on borrowers—give high prominence to the loan-to-value (LTV) ratio at the time of origination. Even a cursory review of publicly available rate sheets shows that LTV and combined LTV (CLTV) ratios, including subordinated financing, can have an impact as large as the change from a 740 credit score to a 620 credit score, all other factors being equal.[36] The Bureau's own primer on setting interest rates confirms this: "In general, a larger down payment means a lower interest rate, because lenders see a lower level of risk when you have more stake in the property."[37]

Creditors emphasize the LTV for three interrelated reasons:

First, borrowers with substantial equity in their home are likely to put their mortgage bill at the top of their pile and do what it takes to keep up with the mortgage, regardless of the impact that may have on their overall finances.

Research by the Urban Institute analyzing the 90-day delinquency rate for GSE loans originated between 1999 and 2016 demonstrates this.[38] For each vintage originated between 1999 and 2016, the delinquency rate for loans with LTVs above 95% was at least 50% greater, and for some vintages as much as 277% higher, than for loans with LTVs below 80%; for the typical vintage, the high LTV loans were more than twice as likely as the low LTVs to reach 90-day delinquency even if the actual serious delinquency incidence has been low by historical standards. Further, as of the time of the Urban Institute's analysis in 2018, the two most recent vintages (loans originated in 2015 and 2016) were the vintages with the largest performance differential; indeed, the 90-day delinquency rate for high LTV loans in the 2016 vintage was 3.7 times higher than for the low LTV loans. This suggests that when delinquency occurs on lower LTV loans it occurs later in the life of the loan, reflecting the efforts borrowers with significant equity (and therefore lower LTVs) make to stay current on their mortgages, whatever the cost to the rest of their lives.

Second, borrowers with significant equity in their home who find that they simply cannot keep up with their mortgage may have an option to refinance to reduce their monthly cost or, at worst, to sell their home, repay the mortgage, and use the equity to purchase a less expensive home or provide a cushion for starting over as a renter. These low LTV borrowers are unlikely to default and allow their property to go into foreclosure (or to provide a deed in lieu), as doing so would cause them to lose much if not all of their equity. Although at one time

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[36] *See, e.g.*, https://www.axosbank.com/-/media/Axos/Documents/rate-sheets/Axos-Bank-Wholesale-Mortgage-Express-Rate-Sheet.pdf (page 1); https://onlineapps.fremontbank.com/Affiliates/Documents/Rates/Wholesale%20Rate%20Sheet.pdf (page 3); https://legacy.unionbank.com/Images/CurrentRateSheet.pdf (page 8).

[37] Bureau of Consumer Fin. Prot. Blog, *Seven factors that determine your mortgage interest rate* (Sept. 29, 2017) https://www.consumerfinance.gov/about-us/blog/7-factors-determine-your-mortgage-interest-rate.

[38] Karan Kaul & Laurie Goodman, Housing Fin. Pol'y Ctr., Urban Inst., *Updated: What, If Anything, Should Replace the Patch* 8 (Oct. 2018), https://www.urban.org/sites/default/files/publication/99268/2018_10_30_qualified_mortgage_rule_update_finalized_4.pdf (drawing calculations from Table 3).

economists had posited that negative equity is a sufficient condition to cause defaults even for those with the ability to repay, recent research strongly suggests that those with negative equity will still seek to avoid foreclosure because of the emotional value of their homes to them.[39] But the recent research confirms that negative equity is, if not a necessary condition for foreclosure, strongly correlated with foreclosure so that the risk of a loan reaching the point of foreclosure is directly related to the LTV.[40]

Third, even if a borrower with significant equity for some reason decides to walk away from the equity and allow the lender to foreclosure and liquidate the property, the lower the LTV, the more likely the lender will be to recover the unpaid principal balance from the sale proceeds.

Setting the loan's price and the creditor's risk of loss will therefore, reasonably, involve a consideration of the borrower's equity. Yet, LTV ratios and the borrower's equity are neither an empirically or statutorily permissible basis for determining ATR. TILA specifically excludes equity-based factors from the ATR analysis.[41] A pricing-based approach, therefore, cannot be the focus of QM, whose purpose after all, is to determine whether the lender presumptively complied with the ATR requirement.

2. Loan factors other than price affect ATR

Even a low-priced loan will be unaffordable if the loan amount is so large or the payment period so short that the monthly payment exceeds the borrower's available income. Loan pricing alone cannot serve to "ensure that responsible affordable mortgage credit remains available to consumers in a manner consistent with the purposes of this section . . . [or] prevent circumvention or evasion."[42]

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[39] *See, e.g.,* Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 35 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), *available at* https://www.nber.org/papers/w21630 (even among borrowers with low equity, almost 96% of borrowers who can afford to pay their mortgages, based on residual income at or above subsistence levels, do so; speculating that attachment to homes could be a contributing factor, among others, in continuing to make payments).

[40] *See, e.g.,* Christopher L. Foote & Paul S. Willen, Federal Reserve Bank of Boston Working Papers, *Mortgage-Default Research and the Recent Foreclosure Crisis* (2017), https://www.bostonfed.org/publications/research-department-working-paper/2017/mortgage-default-research-and-the-recent-foreclosure-crisis.aspx; Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 46 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), *available at* https://www.nber.org/papers/w21630 (showing default increases when homeowners' LTV exceeds 90%, regardless of ability to pay); Laurie S Goodman, Roger Ashworth, Brian Landy and Ke Yin, *Negative Equity Trumps Unemployment in Predicting Defaults*, 19 Journal of Fixed Income 67-72 (2010); Christopher Palmer, *Why Did So Many Subprime Borrowers Default During the Crisis* (Sept. 2015), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2665762; Peter Ganong & Pascal Noel, *Why Do Borrowers Default on Mortgages* (Nat'l Bureau of Econ. Research, Working Paper No. 27585, 2020), https://www.nber.org/papers/w27585.

[41] *See* III.A.2, *supra.*

[42] 15 U.S.C. § 1639c(b)(3)(B)(i).

Absent a requirement to analyze ATR, creditors and others could be incentivized to upsell homebuyers to more expensive houses and larger loans, as lenders, loan brokers, and all the other players involved in closing a mortgage loan generally make more money if the home is more expensive and the loan is larger. Loan pricing, as the sole measure of ability to repay, would provide a safe harbor for asset-based, equity-stripping lending, which are per se predatory practices.[43]

3. Lenders do not always price correctly or fairly

Even if it were correct to substitute the creditor's risk of loss for a measurement of the borrower's ability to repay, basing a presumption of Qualified Mortgage on loan pricing alone requires an assumption that creditors price risk correctly. As the Urban Institute has noted, an assumption that creditors price risk accurately "is hardly assured."[44]

There is compelling evidence that the mortgage market fails to correctly assign prices based on marginal costs and that there is dispersion in price across the mortgage market.[45] The Bureau's own research established that similarly-situated borrowers are being charged different amounts:[46] "Data on daily mortgage rate quotes indicates that the range of interest rates available to a borrower can be significant, even after accounting for loan size and mortgage type."[47] Indeed, the Bureau built and hosts an "Explore Interest Rates" tool for consumers precisely because for any given loan amount, credit score, LTV, and loan type there is a wide range of rates available in any given state.

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[43] *See, e.g.*, 15 U.S.C § 1639b(c)((3)(B)(ii) (giving examples of "predatory characteristics or effects" "such as equity stripping"); 2007 Interagency Statement on Subprime Lending, 72 Fed. Reg. 37569, 37573-574 (loans should be underwritten on ATR, not collateral).

[44] Karan Kaul & Laurie Goodman, Housing Fin. Pol'y Ctr., Urban Inst., *Updated: What, If Anything, Should Replace the Patch* 10 (Oct. 2018), https://www.urban.org/sites/default/files/publication/99268/2018_10_30_qualified_mortgage_rule_update_finalized_4.pdf ("Mispricing could also occur because of perceptions that certain borrowers are riskier or less risky, steering borrowers into high-cost loans, or other market failures. Finally, a rate spread–based regime could give lenders an incentive to price mortgages just below the threshold to qualify for the safe harbor."). *See generally* Nat'l Consumer L. Ctr., Mortgage Lending: Loan Origination, Preemption, and Litigation § 1.3.4 (3rd ed. 2019), *updated at* www.nclc.org/library (discussing the factual evidence demonstrating that credit risk is often not correctly priced for mortgage loans).

[45] NCLC, Mortgage Lending, § 1.3.4.3. *See also* Alexei Alexandrov, Thomas Conkling, & Sergei Koulayex, *Changing the Footprint of GSE Loan Guarantees: Estimating Effects on Mortgage Pricing and Availability* (Dec. 2016), https://editorialexpress.com/cgi-bin/conference/download.cgi?db_name=IIOC2017&paper_id=162 (price dispersion across lenders is roughly 50 basis points, even for prime loans).

[46] Bureau of Consumer Fin. Prot., *Consumers' Mortgage Shopping Experience* (January 2015), https://files.consumerfinance.gov/f/201501_cfpb_consumers-mortgage-shopping-experience.pdf.; . *See also* Alexei Alexandrov, Thomas Conkling, & Sergei Koulayex, *Changing the Footprint of GSE Loan Guarantees: Estimating Effects on Mortgage Pricing and Availability* (Dec. 2016) , https://editorialexpress.com/cgi-bin/conference/download.cgi?db_name=IIOC2017&paper_id=162 (price dispersion across lenders is roughly 50 basis points, even for prime loans).

[47] Bureau of Consumer Fin. Prot., *Consumers' Mortgage Shopping Experience* 8 (January 2015), https://files.consumerfinance.gov/f/201501_cfpb_consumers-mortgage-shopping-experience.pdf.

Fundamentally, loan pricing as a substitute for underwriting was tried once before, and it ended in disaster, for consumers, the secondary market, and the nation's economy, just a decade ago.[48] Creditors have demonstrated conclusively that they cannot be trusted to price loans correctly for credit risk, much less ATR.

C. Default rates are not conclusive proof of ATR

1. The statute looks to ATR, not default rates

In looking to the early delinquency rate on mortgages to assess the affordability of those mortgages, the Bureau implicitly assumes that, if the consumer did not go delinquent during the observation period, the mortgage was "affordable" for the consumer. But that assumption misunderstands the statutory scheme and lacks a basis in empirical observation. Making mortgage payments by itself does not demonstrate ATR, either under the statutory scheme or in reality.[49]

The statutory scheme requires the Bureau to ensure affordable and responsible mortgage lending, but it does not set an acceptable level of default. Nor does it set a time limit past which there is a conclusive presumption of ATR.[50] Rather, creditors are required to assess consumers' ability to repay the mortgage. Under the statute, a consumer has the ability to repay a mortgage if and only if the consumer has the capacity to make the payments on that mortgage and still meet their other preexisting obligations, with enough left over to cover basic living expenses.[51] Thus, the fact that a consumer did not miss two consecutive mortgage payments during the first two years of a mortgage does not in and of itself answer the question of whether the mortgage was affordable when made. Evidence that the consumer struggled with making other debt payments or reduced consumption to subsistence levels or below should be sufficient to establish a lack of ATR, even if the consumer successfully made all the mortgage payments, in full and on time.

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[48] *Cf.*, Edward Goldberg, Richard K. Green & Douglas A. McManus, *Imperfect Information and the Housing Finance Crisis* 11-12 (Feb. 2008), *available at* www.jchs.harvard.edu/research/publications/imperfect-information-and-housing-finance-crisis (describing the dynamic whereby lenders outsourced origination of subprime loans to brokers, who having limited financial and legal risk, cared only about volume; note that the Qualified Mortgage safe harbor repeats this dynamic but in reverse by removing legal risk for failure to underwrite and thus incenting volume production in the Qualified Mortgage space, regardless of other financial or social welfare considerations).

[49] *See, e.g.*, Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 4 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), https://www.nber.org/papers/w21630 ("Specifically, 80 percent of households that need to cut their consumption to subsistence levels to make their mortgage payments ('cant [sic] pay' borrowers) are current on their payments.").

[50] *See* 15 U.S.C. § 1640(k) (providing that borrowers may raise a creditor's failure to make a good faith reasonable determination of ATR as a defense to foreclosure at any time, explicitly overriding the three year statute of limitations for affirmative ATR and TILA rescission claims).

[51] *See, e.g.*, 15 U.S.C. § 1639c(b)A)(vi) (Bureau authority to establish for QM "alternative measures of ability to pay regular expenses after payment of total monthly debt, taking into account the income levels").

2. Borrowers lacking ATR nonetheless pay their mortgages

The reality is that most consumers have multiple obligations and categories of expenses and, when money is tight, they face tough, even agonizing choices. For example, the Federal Reserve Board's 2019 *Survey of Household and Economic Decisionmaking* ("SHED") found that even at the peak of the economic expansion, one in four households went without needed medical care during the prior twelve months because it was unaffordable.[52] The Urban Institute found that a similar percentage faced food insecurity during this time period.[53] The Bureau's own *Making Ends Meet* survey noted that one-third of those who had trouble paying bills also went without food.[54]

Focusing more specifically on homeowners, the Urban Institute's 2017 *Well Being and Basic Needs* survey found that fully 35% of homeowners faced a material hardship during the prior twelve months. Of particular importance, these consumers were almost twice as likely to identify the hardship as an unmet need for medical care and more than twice as likely to identify the hardship as food insecurity than to report the hardship as a partial or late mortgage payment.[55] This underscores the lengths that consumers will go to preserve their homes and the error in the Bureau's assumption that the absence of two consecutive missed mortgage payments equates to affordable payments.

Of course, before having to forego food or medical care, consumers are likely to take other measures to cope with an unaffordable mortgage payment. The *Making Ends Meet* research documented that, when consumers are struggling to pay a particular bill, such as a mortgage payment, a common coping mechanism is to skip or be late in paying another bill.[56] Consistent with that finding, the SHED asked consumers who said that they would not be able to pay all their bills in the month the survey was administered–and 16% of consumers so reported for just that single month–and asked which bill the consumer would be unable to pay. Credit card payments ranked first (45%); followed by phone or cable bills (34%); water, gas and electric bills (32%); and only then mortgage or rent (23%).[57]

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[52] Board of Governors of the Federal Reserve System, *Report on the Economic Well-Being of U.S. Households in 2019* (May 2020), https://www.federalreserve.gov/publications/files/2019-report-economic-well-being-us-households-202005.pdf.

[53] Michael Karpman, Stephen Zuckerman, & Dulce Gonzalez, Urban Inst., *Despite Labor market Gains in 2018, There Were Only Modest Improvements in Families' Ability to Meet Basic Needs* (May 2019), https://www.urban.org/sites/default/files/publication/100216/despite_labor_market_gains_in_2018_there_were_only_modest_improvements_in_families_ability_to_meet_basic_needs_0.pdf.

[54] Bureau of Consumer Fin. Prot., Office of Research, *Insights From the Making Ends Meet Survey* (July 2020), https://files.consumerfinance.gov/f/documents/cfpb_making-ends-meet_survey-results_2020-07.pdf.

[55] Corianne Payton Scally and Dulce Gonzalez, Urban Inst., *Homeowner and Renter Experience of Material Hardship* (Nov. 2018), https://www.urban.org/sites/default/files/publication/99271/homeowner_and_renter_experiences_of_material_hardship_implications_for_the_safety_net_5.pdf

[56] Bureau of Consumer Fin. Prot., Office of Research, *Insights From the Making Ends Meet Survey* (July 2020), https://files.consumerfinance.gov/f/documents/cfpb_making-ends-meet_survey-results_2020-07.pdf.

[57] Board of Governors of the Federal Reserve System, *Report on the Economic Well-Being of U.S. Households in 2019* (May 2020), https://www.federalreserve.gov/publications/files/2019-report-economic-well-being-us-households-202005.pdf.

Researchers have struggled to define what it means for a family not to be able to pay their mortgage.[58] The Bureau could, however, if it chose, make substantial progress on this question using datasets available to it, including the Consumer Credit Panel (CCP) and the National Mortgage Database (NMDB). At a minimum, the Bureau could at least examine correlations between mortgage originations and delinquencies on other types of credit obligations that are visible in credit reporting data in assessing the extent to which mortgages at different price points and DTI levels are consistent with an assessment of the consumer's ability to repay. This data would be highly probative in determining the limits of the Bureau's largely ungrounded assumption that a lack of default on the mortgage payment equals affordability for borrowers. And few outside researchers, and certainly not thinly staffed nonprofits responding to the pandemic, have either the access or the capacity to conduct this research and test the Bureau's conclusory assumptions.[59]

A recent study of consumer "payment hierarchy" by Experian highlights the importance of such an analysis. In that study Experian drew samples of consumers at various points in time and with various combinations of credit obligations and followed those consumers for a period of two years to observe their relative performance on different types of obligations. The findings of the study are striking. For example, with respect to the most recent cohort–those followed from February 2018 to February 2020–Experian found that among those with a mortgage, auto loan, retail card and general purpose credit card, 0.81% became 90 days delinquent on their mortgage whereas five times that number (4.26%) became 90 days delinquent on their bankcard. For those with a mortgage, bankcard, and personal loan, the disparities were roughly the same (1.35% vs. 6.81%).[60] This suggests that originating a mortgage where the consumer lacks a reasonable ability to repay may be manifest in delinquencies on *other* obligations rather than on the mortgage itself.

Looking at the data, we can see that the connection between loan pricing and default rate that the Bureau draws does not address whether the resulting loans are affordable. The

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[58] *See, e.g.*, Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 17 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), https://www.nber.org/papers/w21630 ("It seems reasonable to call a default strategic if a household has free cash flow that exceeds the cost of the mortgage. However, would it be equally appropriate to call a default strategic if the household could only "afford" the mortgage payment by drawing down its retirement savings or borrowing on credit cards? In other words, is default strategic unless the household has exhausted all of its savings and borrowed up to the maximum amount available on all available credit lines?").

[59] *See, e.g.*, Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 17 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), https://www.nber.org/papers/w21630 ("In principle, one could answer this question with data, but to assess the sources of funds for payments, one would need much higher frequency wealth information than the biennial data from the PSID." Note that both the NMDB and the CCP provide the Bureau with access to data much more frequently than biennially.).

[60] Experian, *Consumer payment hierarchy by trade type: Time-series analysis* (July 2020), http://images.go.experian.com/Web/ExperianInformationSolutionsInc/%7Ba6ad2c78-e1da-46eb-b97b-bf2d953ce38d%7D_Payment_Hierarchy_Report.pdf. The Experian report confirms prior research indicating consumers' payment hierarchy are responsive to economic conditions and varied during the Great Recession. *See* TransUnion, *Payment Hierarchy Analysis* (2012), https://www.transunion.com/docs/rev/business/marketperspectives/smallbusiness/Payment_Hierarchy_White_Paper.pdf; TransUnion, *Consumers Place Personal Loans Atop the Credit Mountain* (May 2017), https://newsroom.transunion.com/consumers-place-personal-loans-atop-the-credit-mountain/. The recent Experian report appears to contradict the second of the TransUnion reports.

connection also fails to demonstrate anything about the individual borrower, a necessary element of TILA's ATR provisions. There is no surprise that the data show that consumers are less likely to default if they are paying a lower priced loan.[61] However, whether an individual person can afford a loan or whether that person defaults on a loan depends on many factors and the strain from price is only one of them. Thus, even when creditors correctly predict that a given loan will not default, and are not caught off guard by a subsequent factory closing or other local or national economic shock, that is a separate analysis from whether a particular customer can afford a particular loan.

Research supports our empirical experience: the vast majority of households that cannot afford their mortgages nonetheless keep paying them.[62] Such sacrifices have real life consequences in terms of limiting options for investment in education and retirement and often health and nutrition.[63]

3. Early default is not a reliable proxy for ATR

The Bureau, in basing its assessment of ATR on post-hoc default levels, implicitly assumes that there is some "acceptable" level of default for affordable and responsible mortgages, and that defaults caused by exogenous economic conditions can nonetheless be disentangled from defaults caused by a lack of ATR. Given that the vast majority of borrowers continue making their mortgage payments even when they lack ability to do so,[64] this assumption seems questionable at best. It would be no more defensible to label loan pools above a certain level of default as *prima facie* evidence of unaffordable and irresponsible lending, an approach that rightly would raise very strong objections from creditors and investors.

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[61] *See, e.g.*, Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *The 2006 HMDA Data*, Fed. Reserve Bull. A73, A107 (2007), available at www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf (holding economic factors constant, every 1% increase in high cost lending led to a 0.03% increase in the foreclosure rate for metropolitan statistical area); AARP Public Pol'y Inst., *A First Look at Older Americans and the Mortgage Crisis* 5 (2008), available at https://assets.aarp.org/rgcenter/econ/i9_mortgage.pdf (having a subprime loan increases the risk of foreclosure on average by 14.4%, and by 17% for Americans over 50).

[62] Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 4 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), https://www.nber.org/papers/w21630 ("Specifically, 80 percent of households that need to cut their consumption to subsistence levels to make their mortgage payments ('cant [sic] pay' borrowers) are current on their payments.").

[63] *See*, Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 17 n. 20 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), https://www.nber.org/papers/w21630 ("[A] 'can pay' household is diverting money from saving and, therefore, future consumption by making its monthly payment. If along some future path, such a lack of saving results in destitution, then some 'can pay' households, as we have defined them, really cannot afford their mortgage payments.").

[64] Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 4 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), https://www.nber.org/papers/w21630 ("Specifically, 80 percent of households that need to cut their consumption to subsistence levels to make their mortgage payments ('cant [sic] pay' borrowers) are current on their payments.").

The current economic indicators should be a sufficient reminder that default has far more to do with macroeconomic conditions than individual ATR. Mortgages of a variety of vintages are now 90+ days delinquent, the highest level since the nadir of the Great Recession.[65] The MBA reported that the 4 percentage point rise in the delinquency rates for the second quarter of 2020 was the highest quarterly increase in the survey's history.[66] But no one is ascribing this to a surge of unaffordable lending in recent years. Instead, we accept that this is a consequence of even more historic levels of unemployment.[67]

Default is primarily driven by post-origination events, not foreseeable at the time of origination.[68] The Bureau's reliance on default and delinquency rates as evidence of a lack of ATR risks branding small local lenders suffering a spike in early defaults as a result of a factory closing as irresponsible mortgage originators of unaffordable loans.

4. Consumer harm caused by a lack of ATR occurs independently of pricing

Requiring ability to repay is sound policy. The last crisis was rife with examples of the harm done to consumers by the failure of even reputable, national lenders to consider ability to repay in the absence of an external mandate to do so. Pricing by itself did not prevent a lack of ATR or even early default. The foreclosures sparked by a market-wide lack of ATR included prime loans and near-prime loans, well within the Bureau's proposed pricing band.

Legal aid lawyers and housing counselors who worked with homeowners in the last crisis remember many examples of homeowners in prime or near prime loans who nonetheless faced foreclosure or struggled to make payments because of a lack of ATR. For example, the Atlanta Legal Aid Society, in the years immediately preceding the Great Recession, represented many consumers on fixed incomes who had prime or near-prime mortgages extended to them by national lenders at DTIs ranging from 78% to over 200%.[69] The loans were not high-cost mortgages: some were prime; others near prime. The income was, in most instances, documented in the file. The LTVs ranged from 25% to 81%. In the event of foreclosure, the creditor was well-positioned to recover. But the homeowner had no realistic ability to repay.

[65] Kathy Orton, *Serious mortgage delinquencies soared to a 10-year high last month*, Wash. Post (Aug. 21, 2020).
[66] Kathy Orton, *Serious mortgage delinquencies soared to a 10-year high last month*, Wash. Post (Aug. 21, 2020).
[67] *See, e.g.,* Heidi Shierholz, Econ. Pol'y Inst. Working Economics Blog, *Total initial UI claims have risen in each of the last four weeks* (Sept. 3, 2020), https://www.epi.org/blog/total-initial-ui-claims-have-risen-in-each-of-the-last-four-weeks-congress-must-act.
[68] *See, e.g.,* Kristopher Gerardi, Kyle F. Herkenhoff, Lee E. Ohanian & Paul S. Willen, *Can't Pay or Won't Pay Unemployment, Negative Equity, and Strategic Default* 37 (Nat'l Bureau of Econ. Research, Working Paper No. 21630, 2015), https://www.nber.org/papers/w21630 (residual income at time of default correlated with default, but residual income at time of origination is not well correlated with default).
[69] Comments of the Atlanta Legal Aid Society, Inc., Consumer Federation of America, National Consumer Law Center (on behalf of its low-income clients), the National Association of Consumer Advocates, and the National Community Stabilization Trust on Qualified Mortgage Definition under the Truth in Lending Act (Regulation Z) 84 Fed. Reg. 37,155, Docket No. CFPB–2019–039 at 15 (September 16, 2019), https://www.nclc.org/images/pdf/foreclosure_mortgage/dodd-frank/comments-to-cfpb-qualified-mortgage-sept2019.pdf.

During the bubble years leading up to the crisis, lenders drove up prices on homes by serial refinancing of homeowners from one loan to yet another larger loan. The borrower's ability to repay was often irrelevant because the lender could count on price appreciation to enable refinance flipping, with each successive refinance generating additional income for the creditor. A meaningful ATR regime in the years leading up to the crisis could have prevented this financial harm to borrowers, even though, due to the availability of what seemed like endless opportunities to refinance, there were relatively few defaults, early or not.

And then, when the house of cards came tumbling down in 2007-08, a lack of ATR was revealed not just in loans made in the prior few years but in earlier years as well. While many unaffordable loans do not see early default, many do eventually enter foreclosure—a harm that could have been mitigated in the last crisis with an ATR requirement. And yet now, on the basis of a thin and often ahistorical evidentiary basis, the Bureau proposes to remove this key protection. Removing any requirement to assess for ability to repay would invite a resurgence of abusive lending to our most vulnerable communities and consumers, who have still not recovered from the last crisis, and deprive them of their strongest defense against the loss of their homes. Permitting creditors to take advantage of a safe harbor from liability for violation of the Dodd-Frank Act ability to repay requirements, without some mandated consideration of ability to repay, invites abuse.

D. Use of pricing creates risk

1. The bureau's threshold would insulate loans where a sizable percentage of borrowers lack ATR and would create a heightened risk of foreclosure

The very data the Bureau relies on in trying to establish a link between ATR and early defaults shows how the Bureau's proposed rule would provide liability protection for high-risk loans without a reasonable basis to presume the borrower has the ability to repay.[70]

The Bureau has chosen to look to 60+ day delinquencies occurring during the first two years after origination as a proxy for assessing the ability to repay of borrowers. This metric assumes that every consumer who avoided a 60+ day delinquency during the first two years of origination had the ability to repay the loan, even if the consumer succeeded in staying current on the loan only at great cost. As discussed above, more robust analysis would look at the totality of a borrower's credit obligations post origination to see if the consumer was able to stay current on all loans and would look at a variety of time windows. (A robust analysis also would exclude loans that prepaid within any given time window as the prepayment could mask an inability to make the monthly payments.)[71]

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[70] We note that, to the extent the Bureau relies on litigation risk in establishing the QM safe harbor, its decision to do so is not reasonably supported by any available evidence. Moreover, the Bureau fails to provide a reasoned justification in this regard for its departure from the judgments made in the 2013 Rule. The 2013 Rule demonstrated that any true litigation risk was small.78 Fed. Reg. 6408, 6512 While non-QM lending has not emerged, that does not necessarily mean that the litigation risk is real; indeed, there has been nothing but speculation about litigation risk under ATR for the last seven years.

[71] *See* III.C.2, *supra.*

The data contained in the Bureau's proposal is quite compelling in showing the extent to which it would shelter unaffordable loans. Looking at loans originated between 2002 and 2008–a period that includes pre-crisis loans when credit was quite loose and loans made during the crisis when credit tightened–the Bureau finds that even after excluding loans with "risky" features, at the margin (i.e., at a price of APOR + 175 to 199 bps), 13% of the loans that the Bureau would treat as QM experienced severe early delinquency.[72] That data belies the Bureau's theory that, through the business cycle, lenders accurately assess and price for credit risk (which, to repeat, should not be relevant in any event) and provide an indication of the extent to which the Bureau's proposal would extend a presumption of affordability to loans that were not affordable.

Moreover, the Bureau's analysis is both over-inclusive and under-inclusive. By blending together loans made during two quite different periods, the Bureau's data likely understates the early delinquency rate for loans made prior to the crisis (e.g., between 2002 and 2006). The Bureau should separately analyze those vintages to see what share of borrowers receiving what the Bureau would view as QM loans manifested behavior that the Bureau itself recognizes as indicative of inability to repay.

The Bureau also should analyze the experience of loans with "risky" features. While it is true that such loans cannot be qualified mortgages because of the product feature restrictions in the statute, it was certainly clear that these loans–including loans without documentation or with negative amortization—were riskier loans. If the Bureau's theory about pricing as a measure of ATR were valid, those loans should have been priced above any conceivable QM threshold, because they clearly did not meet the bar of ability to repay.

In addition to the data supplied by the Bureau, other data also indicates that the Bureau's proposed pricing standard would insulate a substantial share of unaffordable loans. The Urban Institute has published reports that examine the "over 90+" delinquency rate for various vintages of GSE originations. This metric, like the Bureau's early delinquency metric, has advantages and disadvantages: on the one hand, it is more likely than the Bureau's metric to capture instances in which borrowers struggled to stay afloat for a period of time on an unaffordable loan before ultimately succumbing, while it is also more likely to capture defaults due to unforeseeable financial shocks occurring years after origination. Because the strengths and weaknesses of this metric counterbalance the strengths and weaknesses of the Bureau's metric, the Urban Institute report provides a useful complement to what the Bureau has analyzed and suggests a complementary analysis that the Bureau itself should perform using its more representative data in the NMDB.

The Urban Institute work shows that, even after excluding loans with non-traditional features, loans originated between 2001-2004 at a price between 151 and 200 basis points above APOR had a 90-day delinquency rate of 20.4%; for GSE loans the delinquency rate was even higher (22.7%).[73] Loans originated between 2005-2008 had a 90+ delinquency rate of 29.2% (and GSE loans a delinquency rate of 36.1).

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[72] 85 Fed. Reg. 41716, 41732 (Table 1).

[73] Karan Kaul & Laurie Goodman, Housing Fin. Pol'y Ctr., Urban Inst., *Updated: What, If Anything, Should Replace the Patch* 9, Table 4 (Oct. 2018),

Both the Bureau's analysis and a separate Urban Institute analysis included in Urban's response to the ANPR also highlight the extent to which the Bureau's proposal, in the name of keeping the QM share of the market constant, fundamentally alters the risk parameters of QM loans. For example, the Bureau's analysis indicates that the early delinquency rate for loans originated between 2002 and 2008 that, at the margin (i.e., at DTIs between 41% and 43%), would qualify as General QM loans was 6% — less than half the early delinquency rate for the marginal QM loan under the Bureau proposal.[74] Similarly, the Urban Institute's response to the ANPR looks at 90+ delinquency rates for Fannie Mae "traditional" loans originated between 1999 and 2018; it shows that using a DTI standard, at the margin (between 40% and 45%) the delinquency rate approximates 3%, half the delinquency rate for the marginal loan under the Bureau's proposal (loans priced at between 151 and 200 bps above APOR).[75] In other words, the Bureau's proposal will predictably insulate from scrutiny much higher levels of unaffordability as measured solely by early delinquency and default rates.[76]

The lesson from these data is clear. If the Bureau desires to eliminate the patch and at the same time define the QM boundary in a way that captures the same share of loans as is captured by the patch, without increasing risk to both borrowers and the larger market, the Bureau needs to go back to the drawing board and identify criteria that will expand the QM boundary without roping in a large share of unaffordable loans. Using pricing as the defining criterion for QM succeeds in proxying the current *size* of the QM market but fails to proxy the *characteristics* of the high-DTI loans that fall within the patch. We offer some suggestions below with respect to a possible approach,[77] although we lack the data assets and analytical resources that the Bureau can–and should–bring to bear on this challenge.

It also is worth noting that adoption of the Bureau's proposal will result in a market where FHA-insured loans that meet FHA's QM test will have been underwritten using a multi-factor approach while QM loans financed through GSE or other channels will not. This bifurcated system will mean potentially significantly disparate standards existing at the same time in the marketplace. It also could mean that like-situated consumers could receive different prices depending on which QM standard a creditor applies, and that pricing may or may not equally reflect that consumer's ability to repay the loan.

2. Use of pricing as an irrebuttable presumption of ATR increases fair lending risk

A focus on pricing as a "holistic" factor either ignores or condones the persistent discrepancies in pricing that have harmed marginalized communities. History is rampant with

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https://www.urban.org/sites/default/files/publication/99268/2018_10_30_qualified_mortgage_rule_update_finalized_4.pdf.

[74] 85 Fed. Reg. 41716, 41733 (Table 3).

[75] Karan Kaul, Laurie Goodman & Jun Zhu, Housing Fin. Pol'y Ctr., Urban Inst., *Comment Letter to the Consumer Financial Protection Bureau on the Qualified Mortgage Rule* (Sept. 2019), https://www.urban.org/sites/default/files/publication/101048/comment_letter_to_the_consumer_financial_protection_bureau_0.pdf.

[76] *See* III.C., *supra.*

[77] *See* IV., *infra.*

examples showing that Black and Latinx mortgage borrowers have paid more for loans than similarly situated White borrowers.[78] In fact, in the years leading up to the financial crisis, studies found that Black and Latinx home buyers were 105 and 78 percent more likely to have high-cost mortgages for home purchases despite controlling for credit score and other key risk factors.[79] And, even in the aftermath of Dodd-Frank, ATR, and the QM safe harbor, studies have continued to confirm that mortgage pricing differences remain even after controlling for credit scores, loan-to-value ratios, the existence of subordinate liens, and housing and debt expenses relative to individual income.[80] These findings suggest an inescapable conclusion: *far too often, mortgage price is both inextricably tied to and illegally rooted in the race of the borrower.*

Thus, the Bureau's price-based approach to QM risks exacerbating racial discrimination in the mortgage market by blessing loans priced below a certain threshold as "affordable" and "responsible" absent any individualized assessment of ATR and without any assurance that mortgage pricing will be free of racial bias.

We expect that, under any pricing thresholds the Bureau sets, borrowers and communities of color will be clustered at the top of the QM band, while White borrowers in predominately White communities will get lower priced QM loans. Such a result would be consistent with recent research from academics at UC Berkeley, who found that mortgage "lenders charge otherwise-equivalent Latinx/African-American borrowers 7.9 (3.6 [for refinance]) bps higher rates for purchase [and] refinance mortgages, costing $765M yearly."[81] Ironically, the higher pricing of QM loans made to people of color likely will be turned into a cudgel to push the Bureau to permit ever-higher pricing thresholds to expand access to credit for communities of color, and, as a result, subject borrowers of color to even higher prices that are unrelated to their actual risk due to ongoing discrimination in the market and the fundamentally flawed nature of the QM pricing construct.

The most recent HMDA data confirm that Black and Latinx borrowers continue to pay more for mortgage credit than whites.[82] Black borrowers, especially, face a much higher priced mortgage market than White borrowers. According to the Bureau's August 2020 analysis of HMDA data, at the median Black and Latinx borrowers pay higher interest rates than White

[78] *See, e.g.,* Robert G. Schwemm & Jeffrey L. Taren, *Discretionary Pricing, Mortgage Discrimination, and the Fair Housing Act*, 45 Harv. C.R.–C.L. L. Rev. 375, 389–390 (2010); Cheryl L. Wade, *How Predatory Mortgage Lending Changed African American Communities and Families*, 35 Hamline L. Rev. 437, 440 (2012).

[79] Patrick Bayer, Fernando Ferreira, Stephen L. Ross, *What Drives Racial and Ethnic Differences in High Cost Mortgages? The Role of High Risk Lenders*, NBER Working Paper No. 22004 (February 2016), *available at* https://www.nber.org/papers/w22004.

[80] *See, e.g.*, Patrick Bayer, Fernando Ferreira, and Stephen L. Ross, *The Vulnerability of Minority Homeowners in the Housing Boom and Bust.* 8 American Economic Journal: Economic Policy, 1-27 (2016).

[81] Robert Bartlett, Adair Morse, Richard Stanton, and Nancy Wallace, *Consumer Lending Discrimination in the Era of FinTech*, (Nov. 2019), available at https://faculty.haas.berkeley.edu/morse/research/papers/discrim.pdf (last accessed 09/08/20).

[82] Feng Liu, Jason Dietrich, Young Jo, Akaki Skhirtladze, Misha Davies, & Corinne Candilis, Bureau of Consumer Fin. Prot., *Introducing New and Revised Data Points in HMDA: Initial Observations from New and Revised Data Points in 2018 HMDA* 58, 63 (Aug. 2019), https://files.consumerfinance.gov/f/documents/cfpb_new-revised-data-points-in-hmda_report.pdf (noting that the elevated denial rates for Hispanics and African-Americans compared to white borrowers hold true even after accounting for credit score).

borrowers.[83] Median Black borrowers pay 25 basis points more for conventional and jumbo conforming loans, 12.5 basis points more for FHA loans, and 12.5 basis points more for the total of all mortgage loans.[84] Black and Latinx borrowers also make up a higher share of higher-priced mortgage loans: "For home purchase loans, 22.9 percent of loans to Black borrowers and 23.7 percent of loans to Hispanic White borrowers were higher-priced, compared with 8.2 percent of loans to non Hispanic Whites."[85]

Although the Bureau did not disaggregate the various credit characteristics of the borrowers in order to assess how much of the discrepancy was directly tied to race and how much was explainable by facially neutral credit characteristics,[86] most attempts to do so have found some amount of pricing disparities that can only be explained by reference to race.[87] For example, a 2020 decision by the Ninth Circuit Court of Appeals that allowed Oakland's claim against Wells Fargo for lost property tax revenue recounted the city's analysis:

> The City's first set of regression analyses support its allegation that Wells Fargo issues predatory home loans to Black and Latino borrowers. According to these studies, a Black Wells Fargo borrower is 2.403 times more likely to receive a predatory loan than a similarly situated White borrower. A Latino Wells Fargo borrower is 2.520 times more likely to receive such a loan than a similarly situated White borrower. Importantly, the first regression analysis controls for independent variables such as objective characteristics like credit history, loan-to-value ratio, and loan-to-income ratio that might contribute to a borrower receiving a predatory loan. In fact, this discrepancy holds true even for more credit-worthy borrowers—Black and Latino borrowers with FICO scores above 660 are, respectively, 2.261 and 2.366 times more likely to receive predatory loans from Wells Fargo than similarly situated White borrowers.[88]

Differences in pricing for Black and Latinx borrowers are not simply a function of objective financial characteristics, even leaving aside the inherent racial disparities built into generational wealth accumulation and supposedly race-neutral credit measures such as credit scores.[89]

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[83]Bureau of Consumer Fin. Prot., *An Updated Review of the New and Revised Data Points in HMDA: Further Observations using the 2019 HMDA Data* 223, Table 7.1.3 (Aug. 2020), https://files.consumerfinance.gov/f/documents/cfpb_data-points_updated-review-hmda_report.pdf.

[84] Bureau of Consumer Fin. Prot., *An Updated Review of the New and Revised Data Points in HMDA: Further Observations using the 2019 HMDA Data* 223, Table 7.1.3 (Aug. 2020), https://files.consumerfinance.gov/f/documents/cfpb_data-points_updated-review-hmda_report.pdf.

[85] Bureau of Consumer Fin. Prot., Data Point: *2018 Mortgage Market Activity and Trends* 47 (Aug. 2019), https://files.consumerfinance.gov/f/documents/cfpb_2018-mortgage-market-activity-trends_report.pdf.

[86] Bureau of Consumer Fin. Prot., *An Updated Review of the New and Revised Data Points in HMDA: Further Observations using the 2019 HMDA Data* 69 (August 2020).

[87] *See, e.g.*, Jung Hyun Choi, Urban Inst., Urban Wire: The Blog of the Urban Institute, *Breaking Down the Black-White Homeownership Gap* (Feb. 2020), https://www.urban.org/urban-wire/breaking-down-black-white-homeownership-gap (finding that 17% of the homeownership gap between Blacks and Whites cannot be explained by income, credit score, marital status, or education).

[88] City of Oakland v. Wells Fargo, --- F.3d ----, 2020 WL 5035815 at *3 (Aug. 26, 2020).

[89] National Consumer Law Center, *Past Imperfect: How Credit Scores and Other Analytics "Bake In" and Perpetuate Past Discrimination* (May 2016), https://www.nclc.org/images/pdf/credit_discrimination/Past_Imperfect050616.pdf.

The Bureau should not accept disparate pricing and build it into the QM structure. Loans priced at APOR and those at 150 or 200 basis points above APOR have meaningful differences—the more expensive loans can place more financial pressure on the borrower. Fair lending, like TILA, requires individualized assessments of risk so that price is truly calibrated to the individual and not to what the market will bear, while secure in the knowledge that neither regulators nor homeowners can peek behind the safe harbor curtain to see the mechanics of racially discriminatory pricing at work.

Moreover, to the extent that the Bureau's proposal would insulate creditors making predictably unaffordable loans from accountability for their failure to make a reasonable and good faith determination of ATR,[90] the consequences of those predictably unaffordable loans will fall heaviest on communities of color, and particularly on African American communities. The foreclosure crisis brought on by the last great wave of irresponsible, unaffordable lending stripped communities of color–particularly Black communities–of more than a generation of wealth.[91] Now, more than a decade since the end of the Great Recession, the divide between White rates of homeownership and Latinx and Black rates has not closed.[92] On the contrary, the homeownership divide between Black and Whites, which had been shrinking for decades before the foreclosure crisis, is now greater than it was during the Jim Crow era.[93] Latinx homeownership has also not reached its pre-crisis levels.[94] The clear majority of White households—76%—live in homes they own. But only 51.4% of Hispanics households and only 47% of African American households live in homes they own.[95]

This large divide in homeownership denies those communities the opportunity for economic mobility offered by homeownership, which provides the ability to build equity, provide stable homes for children, and pass wealth on to heirs. While there are several reasons for this gap, including a wage gap as well as structural discrimination such as that caused by exclusionary zoning, one of the most important reasons for the gap is differential access to responsible, affordable, mortgage credit. Latinx and Black consumers seeking home loans continue to be denied mortgage credit at disproportionately high rates and to be overcharged for

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[90] *See* III.D.1, *supra.*

[91] *See, e.g.*, Dedrick Asante-Muhammad, Chuck Collins, Josh Hoxie, & Emanuel Nieves, Prosperity Now, *The Road to Zero Wealth: How the Racial Wealth Divide Is Hollowing Out the Middle Class* 8 (Sept. 2017), https://prosperitynow.org/sites/default/files/PDFs/road_to_zero_wealth.pdf (showing decline in both African-American and Latino household wealth over the period from 2007-2013 to levels below household wealth thirty years earlier).

[92] Urban Inst., *Nine Charts about Wealth Inequality in America* (Updated) (Oct. 2017), https://apps.urban.org/features/wealth-inequality-charts.

[93] Aaron Glantz & Emmanuel Martinez, *For people of color, banks are shutting the door to homeownership*, Reveal News, Ctr. for Investigative Reporting (Feb. 15, 2018), https://www.revealnews.org/article/for-people-of-color-banks-are-shutting-the-door-to-homeownership/; Urban Inst. Data Talk, *Black-White Homeownership Gap: A Closer Look Across MSAs* (June 2019), https://www.urban.org/sites/default/files/2019/07/16/black_homeownership_data_talk_slides.pdf (slide 27).

[94] Unidos US, Fact Sheet, *Latino Homeownership Hanging in the Balance: Observations from the Home Mortgage Disclosure Act* (Mar. 2018), http://publications.unidosus.org/bitstream/handle/123456789/1838/Latino%20HMDA%20Fact%20Sheet.pdf?sequence=4&isAllowed=y.

[95] U.S. Census Bureau, Quarterly Residential Vacancies and Homeownership, Second Quarter 2020, CB20-107at 9 (July 28, 2020), https://www.census.gov/housing/hvs/files/currenthvspress.pdf.

the mortgage credit they do receive.[96] The most recent HMDA data confirm that Latinx and Black applicants are denied at rates higher than Whites, even accounting for credit score, and pay more for every kind of mortgage loan reported under the HMDA data.[97]

The Bureau has a special statutory responsibility to ensure fair lending. Among the Bureau's objectives is protecting consumers from discrimination.[98] And Congress specifically charged the Bureau with "ensur[ing]" access to "responsible, affordable mortgage credit"[99] that "reasonably reflect[s] . . . ability to repay."[100] While the Bureau has an obligation to do so for all consumers, the statute intentionally required the Bureau to focus on "traditionally underserved consumers and communities,"[101] which includes communities of color. Yet, the negative risks inherent in the Bureau's currently proposed QM pricing approach—of enabling some level of pricing discrimination and sheltering some level of predictably unaffordable mortgage lending—will likely be concentrated in communities of color. Accordingly, the proposed rulemaking, in its current state, appears to be in direct contradiction with the Bureau's statutory obligations to protect borrowers and communities of color from discrimination in the mortgage market by ensuring their access to responsible, affordable mortgage credit.

Given these concerns and the Bureau's statutory obligations, it is imperative that the Bureau assess and empirically evaluate the fair lending risk created by and embedded in its proposed pricing threshold for QM loans before adopting any final regulation. For example, using the National Mortgage Database, the Bureau should be able to disaggregate its analysis by race and nationality to assess the extent to which, at any given price band (and especially at the margins), early delinquency rates are consistent for White, Black and Latinx consumers. Disparities in those delinquency rates could suggest that the "holistic" nature of pricing actually encompasses invidious factors. Without such analysis, however, the Bureau falls far short of its statutory mandate to promote fair lending and shelter traditionally underserved communities from unfair, discriminatory, and abusive credit practices.

3. Pricing exacerbates risks from both market expansions and market contractions

The pro-cyclical nature of the Bureau's proposal may facilitate more unaffordable loans and fail to impose necessary guardrails against systemic risk. As the Bureau's proposal notes, "[A] rate spread-based QM threshold would likely be less effective in limiting risky loans

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[96] Bureau of Consumer Fin. Prot, *Data Point: 2017 Mortgage Market Activity and Trends* 41, 50 (May 2018), https://files.consumerfinance.gov/f/documents/bcfp_hmda_2017-mortgage-market-activity-trends_report.pdf. (reporting that Black borrowers are denied loans at more than twice the rate of White borrowers, and Latinx and Black borrowers are more than twice as likely as White borrowers to have high-priced loans as well).
[97] Feng Liu, Jason Dietrich, Young Jo, Akaki Skhirtladze, Misha Davies, & Corinne Candilis, Consumer Fin. Prot. Bureau, *Introducing New and Revised Data Points in HMDA: Initial Observations from New and Revised Data Points in 2018 HMDA* 58, 63 (Aug. 2019) (noting that the elevated denial rates for Latinx and Black borrowers compared to White borrowers hold true even after accounting for credit score).
[98] 12 U.S.C. § 5511(b)(2).
[99] 15 U.S.C. §§ 1639b(a)(1), 1639c(b)(3)(B)(i).
[100] 15 U.S.C. § 1639b(a)(2).
[101] Dodd-Frank Act § 1013(b)(2) (creating the unit of Community Affairs). *See also* Dodd-Frank Act § 1013(c) (creating the Office of Fair Lending and Equal Opportunity).

during periods of strong housing price growth or encouraging safe loans during periods of weak housing price growth."[102] This concern requires serious attention.

The Bureau's removal of DTI threatens systemic risk. As discussed in a recent paper by Patricia McCoy and Susan Wachter, the lack of an external DTI mandate will incentivize lenders to remove their own internal underwriting caps during an inflating housing bubble in order to compete for loans.[103] "Investors are not able to observe the compensating factors, and compensating factors (soft data) override the safety constraints that DTI (hard data) would provide. . . . As the current system worsens, so does the potential for destabilization from banks to nonbanks."[104] The Bureau's pricing proposal does not replace DTI with an adequate measure to protect against such systemic risk. As we learned in the last crisis and the devastation that followed, such measures are necessary, and the Bureau must provide them.

4. Increases in the pricing threshold would increase risk of consumer harm

A tight pricing cap might encourage downward pressure on pricing, but we believe the Bureau will face constant pressure to adjust any pricing cap upward in order to capture the maximum universe of potentially affordable loans, whether they are indeed either affordable or responsible. The larger the potential band, the greater the risk of adverse fair lending consequences, unaffordable loans, and acceleration of market cycles. We are aware that already there is significant pressure to raise the safe harbor threshold in the name of expanding access, coupled with assertions that doing so would only increase the default rate by a few percentage points. But each increase in the risk of foreclosure will, we know, fall disproportionately on communities of color, as communities of color receive the most expensive and riskiest loans and often also have the hardest time avoiding foreclosure.

As price increases, so too does the risk that the loan has been subject to abuses including discrimination, upcharging and other predatory practices. It is commonly known that after the high-cost mortgage protections were passed under the Home Ownership and Equity Protection Act ("HOEPA"), subprime lenders routinely priced loans to fall just below the HOEPA threshold, not because risk-based pricing called for such a price, but because the goal was to charge as much as possible while avoiding extra legal obligations for the lender.[105] If the Bureau increases the level to 200 basis points above APOR, the market will respond with more of these high-priced loans even for borrowers whose profile qualifies them for lower priced loans. And, historically, the people and communities that have been sold loans at inflated prices, are people and communities of color, primarily Black, Latinx, and Native American people and communities.[106]

[102] 85 Fed. Reg. 41716, 41736.
[103] Susan M. Wachter and Patricia A. McCoy, *The Macroprudential Implications of the Qualified Mortgage Debate*. 83 Journal of Law & Contemporary Problems 21-47 (2020).
[104] *Id*. at 26.
[105] *See, e.g.*, Neil Bhutta, Jack Popper, & Daniel R. Ringo, *The 2014 Home Mortgage Disclosure Act Data*, Federal Reserve Board Bulletin (Nov. 2015), https://www.federalreserve.gov/pubs/bulletin/2015/pdf/2014_HMDA.pdf.
[106] *See, e.g.*, Marsha J. Courchane, *The Pricing of Home Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?*, 29 J. Real Estate Res. 399 (2007) (African Americans more than two and a half

It is important to note that these decisions are not made in the context of a pure and transparent marketplace. Indeed, the relationship between borrower and creditor is highly asymmetric when it comes to pricing. Consumers have little understanding or insight into the factors a creditor uses to offer a loan. In many cases, and particularly in communities of color, shopping among creditors is not uniformly practiced by prospective borrowers. This leaves consumers exposed to opaque price quotes that, absent insight into the factors or how like-situated borrowers are being priced by the same or other creditors, provide little room for informed negotiation or price shopping. In other words, creditors have the upper hand and there is no reason to assume a real negotiation, with downward pressure on prices, is occurring.

Given that the Bureau implicitly recognizes that increasing price increases risk for borrowers and that borrowers have little leverage over the price of credit in the course of a mortgage negotiation, the Bureau should maintain the risk as low as possible if it is going to ensure affordable and responsible mortgage lending.

At the time Congress passed the Dodd-Frank Act, the Federal Reserve Board had already established ATR rules for higher-priced mortgage loans. A safe harbor set at 150 basis points returns us largely to the state of the world at the time Congress passed the Dodd-Frank Act, with loans 150 basis points above APOR subject to a rebuttable presumption and loans below the trigger effectively safe harbored. Moving the safe harbor higher expands the costliness of loans whose affordability and responsibility is conclusively presumed beyond the presumption in place when Congress passed the Dodd-Frank Act. The Bureau's proposal fails to give effect to Congressional intent in passing the Dodd-Frank Act.

To the extent the Bureau is contemplating creating a mechanism through which it can, going forward, change the pricing threshold on the QM rule on an "emergency" basis without notice and comment rulemaking, we urge against such a measure. If the Bureau nevertheless establishes such a rule, any special emergency powers should be extremely circumscribed, with

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times as likely and Hispanics roughly twice as likely as Whites to receive a subprime loan); Thomas P. Boehm, Paul D. Thistle, & Alan Schlottman, *Rates and Race: An Analysis of Racial Disparities in Mortgage Rates,* 17 Housing Pol'y Debate 109, 126 (2006) (finding that African Americans in the conventional market pay 20 basis points more for purchase loans and 94 basis points more for refinances, and Latinos pay 12 basis points more for purchase loans, than Whites with similar income and education); First Nations Dev. Inst., *Borrowing Trouble: Predatory Lending in Native Communities* 14-16 (2008), *available at* www.firstnations.org/publications/BorrowingTroubleFinalWebv031308.pdf (American Indians receive subprime loans at roughly twice the rate Whites do); Carsey Inst., *Subprime and Predatory Lending in Rural America: Mortgage Lending Practices That Can Trap Low-Income Rural People,* Pol'y Brief No. 4 (2006), *available at* www.carseyinstitute.unh.edu/documents/PredLending.pdf (rural Latinos, Native Americans, and African Americans all disproportionately receive subprime loans, with African Americans nearly three times as likely as Whites to receive subprime loan); Howell E. Jackson & Laurie Burlingame, *Kickbacks or Compensation: The Case of Yield Spread Premiums,* 12 Stan. J.L. Bus. & Fin. 289, 350 (2007) (Black and Latinx borrowers pay more, on average, in broker compensation than Whites); Robert B. Avery, Kenneth P. Brevoort & Glenn B. Canner, *Higher Priced Home Lending and the 2005 HMDA Data,* Fed. Res. Bull. A123, A157-A158 (2006) (pricing disparities between whites and minorities highest for broker originated loans); Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. for Responsible Lending, *Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages* 21-23 (May 31, 2006); Elvin K. Wyly, Mona Atia, Holly Foxcroft, Daniel J. Hamme, & Kelly Phillips Watts, *American Home: Predatory Mortgage Capital and Neighbourhood Spaces of Race and Class Exploitation in the United States, 88 Geografiska Annaler, Series B: Human Geography* 105 (2006); Binyamin Appelbaum & Ted Mellnik, *The Hard Truth in Lending,* Charlotte Observer, (Aug. 28, 2005), at 1A.

at least three limitations: a) a time limit after which the rule can only be continued through a full notice and comment rulemaking; b) a limit on the circumstances when such an act could be undertaken, perhaps tied to data on early defaults and similar loan performance indicators; and c) a limit on how much the Bureau could increase the threshold, in total and at any one time without further review. The data at present are insufficient to provide specific time frames for these potential guidelines.

IV. A hybrid approach would more closely approximate ATR

If the Bureau insists on proceeding with a QM rule that allows the patch to expire without further research, a hybrid approach that incorporates both DTI and price better meets the goal of the statute than either the current proposal or a pure DTI-based approach and better fits with the data the CFPB has provided. It also better aligns with the requirement in 15 U.S.C. §1639c(b)(2)(A)(vi) to consider a borrower's individual ability to repay in connection with income. We recommend that the Bureau expand the General QM definition to include loans with a DTI ratio of up to 45%, using the current dividing line between safe harbor and rebuttable presumptions QMs.

We further recommend that the Bureau consider expanding the rebuttable presumption QM boundary to include loans with a higher DTI and low pricing and do so in such a way that does not materially increase the share of loans that prove unaffordable. For example, based upon the data set forth in the Bureau's proposal, the Bureau could consider treating loans with a DTI up to 48% and a price at or below APOR plus 100 basis points as rebuttable presumption QM loans.[107] This hybrid approach, which is line with the approach on which the Bureau sought comment, would ensure that as the Bureau expands the QM boundary to encompass higher DTI loans the Bureau would not rope in loans which experience demonstrates are often unaffordable. This approach also would assure that homeowners receiving more expensive loans have the benefit of a direct affordability protection rather than being presumed to be able to afford the loan due solely to the loan price.

If the Bureau decides to allow the patch to expire during the pandemic and absent the necessary data analysis described above, a hybrid DTI/pricing model fits its available data far better than its current proposal. By making DTI an explicit component of ability to repay, it fits Congressional intent for the Truth in Lending Act, which explicitly references DTI at several points and prevents the Bureau from promulgating a rule that predictably insulates unaffordable loans by deeming them as meeting the ATR standard.

To begin with, the Bureau should expand the current general GM definition to encompass loans with a DTI of up to 45%. In selecting the 43% limit in the 2013 rule the Bureau acknowledged that "there is no 'magic number which separates affordable from unaffordable."[108] The Bureau chose 43% because it believed at the time that 43% "generally comports with industry standards and practices for prudent underwriting." Specifically, the Bureau asserted that

[107] 85 Fed. Reg. 41716, 41733 (Table 5).
[108] 78 Fed. Reg. 6408, 6527.

"43 percent is the threshold used by the FHA as its general boundary,"[109] although the Bureau believed that the GSEs were using a lower (36%) ratio without compensating factors. However, as the Bureau now recognizes, FHA in fact will guarantee loans up to a 57% DTI and more than half of their loans have DTIs above 43%. Further, the GSEs do not require compensating factors for loans with DTIs up to 45% (and have at times established an even higher threshold before requiring compensating factors). Thus, the premise on which the 43% threshold was chosen seems difficult to defend, and an expansion to 45% would be more in keeping with "industry standards and practices for prudent underwriting."[110] Increasing the DTI threshold to 45% would include at least 30% of the potentially displaced loans resulting from the expiration of the patch.

If the Bureau were to increase the QM threshold above 45%, "industry standards and practices for prudent underwriting" would dictate that the Bureau should identify some additional indicia of affordability to warrant a presumption that the lender reasonably determined the borrower's ability to repay. Although we believe that the most appropriate indicia are those that relate directly to the consumer's financial capacity and that the Bureau should take the time and do the research to define such factors in an objective and administrable manner, we recognize that the current NPRM does not appear to leave room for that approach. Within those constraints, we believe that it is possible to fashion a price-based threshold for higher DTI loans, but at a significantly lower price point than the Bureau has proposed.

To do so, we urge the Bureau to focus on data with respect to the performance–or at least the early delinquency performance–of loans originated during the period from 2002 to 2005. That was a period when the mortgage market was overheated, to put it mildly, and when the protections of an ATR rule were needed; the absence of such a rule led to disastrous consequences. Taking a 45% DTI QM threshold as the baseline, the Bureau could calculate the early delinquency rates for loans at the margin of that threshold (e.g., loans with a DTI of 44% to 45%) and then conduct an analysis similar to the analysis in Table 5 of the proposal to identify cells in which the DTI and price combined produced comparable performance.[111]

By way of illustration, using Tables 4 and 5–which unfortunately include loans originated in 2006-2008 as the crisis was unfolding and credit tightening–it appears that loans with DTIs near 45% had an early delinquency rate of 7%.[112] Loans with a DTI between 46% and 48% which were priced below 100 basis points above APOR had a similar early delinquency rates, as did loans with a DTI between 49% and 50% which were priced below 75 basis points above APOR. If those results held up for data drawn exclusively from the pre-crisis period, the Bureau could consider expanding QM along these lines. While basing such a decision on default rates may lend some credence to a rebuttable presumption standard, we distinguish this approach from using early default rates to provide a full safe harbor from ATR liability.

Importantly, we do not believe that for any loan with a DTI above 45% a lender should be conclusively presumed to have satisfied the ATR obligation where price and DTI are the sole determinants of QM status. The very fact that the DTI exceeds 45% raises some question

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[109] 78 Fed. Reg. 6408, 6505.
[110] 78 Fed. Reg. 6408, 6527.
[111] 85 Fed. Reg. 41716, 41733 (Table 5).
[112] 85 Fed. Reg. 41716, 41733 (Tables 4 and 5).

as to whether the lender made a reasonable determination of the consumer's ability to repay. The fact that the lender offered a low price does not necessarily resolve that question, since the price may reflect the equity in the property or other credit risk characteristics that have nothing to do with the affordability of the loan, even if the creditor correctly priced the credit risk.[113] Thus, we believe that any expansion of QM along these lines should be an expansion of the scope of the rebuttable presumption and not the safe harbor. FHA's rule, in contrast, provides QM status only for a much more multi-faceted analysis.

We recognize that the hybrid approach outlined in the Bureau's proposal did envision some expansion of the safe harbor. But looking at Table 5, what the Bureau suggested would have resulted in loans in the 2002-2008 vintages which, at the margin, produced a 12% early delinquency rate (i.e., loans with DTIs between 46% and 50% and a price between 125 basis points above APOR and 149 basis points above APOR) being conclusively presumed to be within the borrowers' ability to repay. A 12% early default rate cannot be consistent with a conclusive presumption of ATR.

V. Absent data showing that higher-priced small dollar loans have improved ATR compared to other higher-priced mortgages and are both affordable and responsible, the Bureau should not set an inflated threshold for small dollar loans

For loans between $65,939 but less than $109,898, the Bureau proposes a QM threshold of 350 basis points above APOR. The level is 650 basis points above APOR for loans under $65,939. The Bureau provides no empirical basis for this elevated pricing on loans largely made to vulnerable and marginalized communities. The Bureau should align the APOR threshold for small mortgage loans with other loans, in the absence of any data demonstrating that small dollar mortgage borrowers—who tend disproportionately to be lower-income whites and African Americans, Latinx, and Native American borrowers, of all income levels—can afford higher pricing levels better than their relatively more affluent and less discriminated against peers. There seems no basis for presuming that loans made at a higher price to a more vulnerable population reflect ATR as well as cheaper, more mainstream loans. Nor is it easy to see how high-priced small dollar loans are as "affordable" and "responsible" as cheaper, larger loans.

As discussed above, the Bureau may adjust QM only if doing so reflects a basis for presuming an improved ATR assessment. Congress provided express authority to the Bureau to adjust the points and fees cap for smaller loans in order to promote access "in rural areas and other areas where home values are lower."[114] But it did not provide any other general exception authority to the Bureau regarding adjustments to the QM definition for small dollar loans. Unlike the statutory QM safe harbor for loans made by smaller creditors,[115] there is no general QM adjustment for small dollar loans. Therefore, the Bureau may only consider factors relevant to ATR in adjusting the QM definition for small dollar loans and must establish an evidentiary basis for any adjustment. The creditor's cost or profit margin is not a permitted

[113] *See* section III.
[114] 15 U.S.C. § 1639c(b)(2)(D)
[115] 15 U.S.C. § 1639c(b)(2)(F).

basis for an adjustment of the QM definition for small dollar loans, absent a showing that the credit made available is both "affordable" and "responsible."

The demand for smaller dollar loans is concentrated in vulnerable and marginalized communities. The need for smaller dollar real-estate secured loans is especially acute in Black neighborhoods.[116] In recent years, land installment contacts with loan pricing in the range of the Bureau's proposed QM threshold have entered this market—and ruined people's financial lives.[117] Rather than supplanting such toxic and predatory products with the desperately needed affordable, responsible mortgage credit, the Bureau's proposal would bless them and insulate them from liability. Indeed, successful law suits by Atlanta Legal Aid and others against the purveyors of these toxic loans would have been hampered had the Bureau's proposal been in effect.

Manufactured home buyers also disproportionately rely on small-dollar loans. According to the Census, the average price for a new manufactured home, without land, was about $81,000 in 2019.[118] These are by definition not buyers with high wealth or residual income to insulate them from the risks of inflated pricing. The majority of homes are financed with personal property, or chattel, loans. Concerns about collateral depreciation reflect the lack of an upside for borrowers as much as any increased risk for creditors. And the summary repossession rules in many states mean that borrowers can come home to a vacant lot.

The Bureau's data reveal the toxicity of its proposal on these vulnerable and marginalized communities. Table 5 shows that, at any DTI level above 26%, the early delinquency rate for loans priced at 225 basis points above APOR and higher reaches double digits.[119] It climbs to between 16-19% for DTIs between 40 and 50. The table stops at 225 basis points and does not break out the delinquency rate at prices nearing 350 or even 650 basis points above APOR. Before the Bureau can presume that the default levels on loans more than 225 basis points above APOR even suggest ATR, the Bureau should look at the data and make its analysis publicly available for comment.

The Bureau claims that other data demonstrate that smaller loans with higher prices perform similarly to larger loans with lower rates. The analysis it provides, however, does not provide a reasonable basis for including such loans in QM, even with a rebuttable presumption. Table 9, on which the Bureau relies, fails to show how many of the higher priced loans are part of the analysis.[120] Rather than break the higher priced loans out separately to show the default rate, it evaluates a band of loans ranging from 1.5 to 2.0 percentage points above APOR and then increases the band to include loans ranging from 1.5-6.5 percentage points above APOR without any further stratification. If there are comparatively few loans in the bands between

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[116] Matthew Goldstein, *Where a Little Mortgage Goes a Long Way*, New York Times (Aug. 2, 2020), https://www.nytimes.com/2020/08/02/business/mortgages-affordable-housing.html; Alanna McCargo, Bing Bai, Taz George, & Sarah Strochak, Urban Inst., *Small-Dollar Mortgages for Single-Family Residential Properties* (Apr. 25, 2018), https://www.urban.org/research/publication/small-dollar-mortgages-single-family-residential-properties (lack of small dollar lending suppressing Black homeownership).

[117] Matthew Goldstein and Alexandra Stevenson, *Market for Fixer-Uppers Traps Low-Income Buyers*, New York Times (Feb. 20, 2016).

[118] http://www2.census.gov/programs-surveys/mhs/tables/time-series/sitebuiltvsmh.xlsx (Cost and Size Comparisons, New Manufactured Homes and New Single-Family Site-Built Homes).

[119] 85 Fed. Reg. 41716, 41733 (Table 5).

[120] 85 Fed. Reg. 41716, 41758 (Table 9).

200 and 650 basis points above APOR, even if all the loans in those bands fail, the overall default rate will not change much.

If the Bureau seeks to create a higher threshold for the QM pricing rule for smaller loans it must be based on data regarding the affordability of such loans (as measured through various metrics of loan performance) as a category or set of categories using stratified data. The limited public data available suggests that these smaller dollar loans do not perform well, contrary to the Bureau's assertions, at least not when priced at the levels the Bureau is proposing to bless. For example, in 2015, the Seattle Times reported that 28% of chattel loans fail to perform.[121]

As with other pricing thresholds, the Bureau must be careful about where it sets the limit. A sufficiently low level could encourage lower-cost lending, but a level that is too high will simply encourage exploitative lending right under the threshold. In 2014, the Bureau adopted high-cost loan definitions for home loans, with special carve outs for manufactured home loans. For all home loans over $50,000, a high-cost loan is defined as prices at 650 basis points or more above APOR. For manufactured home chattel loans less than $50,000, the threshold is 850. Prior to this rule, the manufactured home loan sector underwrote loans that exceeded these thresholds as a matter of course; starting in 2014, the industry priced nearly all loans below these thresholds.

A review of 2017 HMDA data for the nation's largest manufactured home loan lender found that nearly 20% of its loans between $50,000 and $66,000 (the high-cost definition floor and the QM proposal ceiling for the smallest loans) had a rate spread of either 6.48 or 6.49%.[122] This suggests that many loans were priced to avoid the high-cost designation, but still well above the APOR. Setting the QM line at 650 basis points would encourage this very high-cost lending without any showing whatsoever that the pricing reflects ATR or indeed anything other than the lender's desire to price what the market will bear, with limited legal exposure.

The information provided in the rulemaking does not support the rule as proposed. Instead, it further obscures the relationship between pricing and risk and between pricing and ATR for small dollar loans. Until the Bureau can provide a public basis, based on ATR and affordable and responsible lending, not creditors' profit margins, for charging small dollar loan borrowers more than other borrowers, its proposed rule cannot withstand scrutiny. The much higher small mortgage lending threshold would exacerbate concerns regarding higher priced credit to Black and Latinx homeowners who may need lower dollar loans to buy homes and introduce unwarranted risk into the QM rule for the most vulnerable borrowers.

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[121] Mike Baker & Daniel Wagner, *The mobile-home trap: How a Warren Buffett empire preys on the poor*, The Seattle Times (Apr. 2, 2015), https://www.seattletimes.com/business/real-estate/the-mobile-home-trap-how-a-warren-buffett-empire-preys-on-the-poor/

[122] This analysis of 2017 HMDA Data was done by Prosperity Now.

VI. Consider and verify requirements are an essential component of any ATR protections

A. The Dodd-Frank Act requires creditors to consider and verify debts and income, as no doc loans fueled the last crisis.

The ATR provisions of TILA require creditors to both "consider" and "verify" debts and income as part of their reasonable, good faith determination of ATR. Price by itself is no indication that a lender has done either. Indeed, available rate sheets indicate that consideration and verification of debts and income is entirely irrelevant to pricing.[123] In order to justify a presumption–and especially an irrebuttable one–the lender must show that it considered and verified. Indeed, with respect to income, it would make nonsense of the statute to say that the lender must show that the lender documented income but could then claim a presumption of compliance if the record showed that the lender ignored the evidence, by, for example, documenting a borrower's Supplemental Security Income and selling a loan whose monthly payments equaled the entire amount of that income. Consideration and verification of both debts and income are central to ensuring ATR and must be reflected before ATR can be presumed.

Consider comes first in the statute, followed by verify. In 15 U.S.C. § 1639c(a)(3), the statute provides:

> A determination under this subsection of a consumer's ability to repay a residential mortgage loan shall include **consideration** of the consumer's credit history, current income, expected income the consumer is reasonably assured of receiving, current obligations, debt-to-income ratio or the residual income the consumer will have after paying non-mortgage debt and mortgage-related obligations, employment status, and other financial resources other than the consumer's equity in the dwelling or real property that secures repayment of the loan. A creditor shall determine the ability of the consumer to repay using a payment schedule that fully amortizes the loan over the term of the loan.[124]

In addition, in response to predatory and problematic practices in the pre Dodd-Frank market, the law explicitly requires creditors to "verify amounts of income or assets that such creditor relies on to determine repayment ability. . . ."[125]

Congress reaffirmed the centrality of "consider and verify" requirement by repeating it in the QM safe harbor for small creditors.[126] There should therefore be no question but that creditors who wish to receive the benefit of an irrebutable presumption that a loan complies

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[123] *See* https://www.axosbank.com/-/media/Axos/Documents/rate-sheets/Axos-Bank-Wholesale-Mortgage-Express-Rate-Sheet.pdf (page 1); https://onlineapps.fremontbank.com/Affiliates/Documents/Rates/Wholesale%20Rate%20Sheet.pdf (page 3); https://legacy.unionbank.com/Images/CurrentRateSheet.pdf (page 8). *See also* § II.B.1.a.
[124] 15 U.S.C. § 1639c(a)(3) (emphasis added)
[125] 15 U.S.C. § 1639c(a)(4).
[126] 15 U.S.C. § 1639c(b)(2)(F)(ii)(I)(ee) (requiring small creditors, in order to take advantage of the small creditor QM safe harbor, to "consider[] and document[]the debt, income, and financial resources of the consumer."), *added by* Pub. L. No. 115-74, tit. I, § 101,.132 Stat. 1297 (2018).

with ATR consider and verify both debts and income, as well as other financial resources of the borrower.

The CFPB asks whether it should provide examples of what it means to "meaningfully" consider and verify income. Yes, the Bureau should do that. At minimum, in order to provide some clarity for both consumers and industry, the Bureau should provide examples of clearly bad underwriting practices. Examples of behavior that falls outside the scope of a reasonable "consider" and "verify" analysis provide an uncontroversial outer bound for responsible mortgage lending. Lenders should have systems in place that at a bare minimum catch such behavior.

The law clearly requires an individualized assessment of ability to pay for each and every loan. Even if the Bureau adopts a pricing-based model for QM, it must still maintain the ability to confirm creditors' compliance with the law in conducting a good faith and reasonable determination of ATR. The Bureau must maintain the power to do this through its supervision powers even if individual homeowners who have been harmed are unable to do so due to a safe harbor. The Bureau must affirm, as Congress did, that there can be no QM safe harbor without consider and verify.

B. Joint civil rights-consumer advocates' "consider and verify" term sheet

We have attached a list of principles that civil rights and consumer advocacy organizations have agreed upon as a meaningful standard for the "consider and verify" requirements, including what might be its outer bounds.[127] This document lays out concerns that are held by all the groups signing the document. The practices prohibited by its terms are ones that are per se inconsistent under any circumstances with responsible and affordable lending and therefore should be banned. The concerns therefore are bright lines beyond which no reputable lender would or should go.

As outer bounds, however, they do not define best practices or prudent practices for consider and verify. Falling within these outer bounds should not be taken as conclusive proof that the creditor has complied with the statutory requirements to consider and verify the consumer's debts and income. Nor should a creditor's meeting of these minimal requirements prevent an examiner from assessing whether the creditors' practices, when taken as a whole, comply with the statutory requirements to consider and verify debts and income. But they provide clarity for lenders without resurrecting the ossified and complex detail of Appendix Q.

Below we highlight a few principles from the term sheet.

1. Pricing cannot be used to undermine fair lending

As we discuss above, the risks of a pricing regime are particularly pronounced for communities of color, given the historical prevalence of racial pricing disparities and outright

[127] See Attachment A.

racial discrimination in the mortgage lending market.[128] The Bureau must be unequivocal that its blessing of subprime loans as responsible and affordable under the QM definition does not make those loans either responsible or affordable for purposes of federal fair housing and fair lending laws or state laws governing the provision of mortgage credit. The Bureau should take additional steps to prevent its revised QM definition from being used as shelter for pricing discrimination, including providing that pricing discrimination results in a loss of the QM safe harbor.

2. In order to sustain the presumed link between early defaults and ATR, both the Bureau and creditors should monitor early defaults

In any system the Bureau implements, it must evaluate the effectiveness of the proposal using comprehensive data. In its QM proposal, the Bureau has highlighted early defaults as a key performance indicator. It should monitor that data point to see how loans perform, especially at different pricing ranges. Creditors too should be able to demonstrate that they are monitoring early defaults in order to assess whether ATR is or is not implicated in any unusual spike in early defaults. Where the creditor determines that a lack of ATR is the cause of spikes in early default rates, responsible mortgage lenders will want to make adjustments to ensure they are making a good faith and reasonable determination of ATR going forward.

3. Asset-based lending is a per se predatory practice

TILA provides that in making the repayment ability determination, creditors must not consider the consumer's equity in the dwelling or real property that secures loan repayment.[129] This provision seeks to prevent the practice of loan flipping, a commonplace practice in the last several decades that resulted in the diminished equity of many long-time homeowners.[130] Loan flipping involves repeated refinancings, often close in time, where the financed closing costs are paid immediately to the creditor (or broker). Such loans are enabled by the existing equity in the home.

4. In order to maintain the safe harbor, creditors must retain documentation

The Bureau should state that in order to retain the safe harbor, lenders must retain specified documents to demonstrate upon review how it satisfied "consider" and "verify." Lenders who do not wish to retain documentation—because they find it unduly burdensome or because they believe sufficient time has elapsed that ATR has been established—could destroy documentation, without penalty. However, should a question arise as to whether or not there

[128] *See* 15 U.S.C. § 1639c(a)(3); *see also* III.D.1, *supra.*
[129] *See generally* III.A.2III.A.2
[130] For a discussion of loan flipping, see Kathleen C. Engel & Patricia A. McCoy, *The Subprime Virus* 23 (Oxford University Press 2011); Hearing, U.S. Senate Special Committee on Aging, *Equity Predators: Stripping, Flipping and Packing Their Way to Profits* (March 31, 1998).

was ATR on the loan, the creditor would not be able to avail itself of the safe harbor. The borrower still would be able to make an inquiry into the lender's good faith determination of ATR.

Examiners will also want an ability to assess whether the creditor meaningfully considered and verified borrowers' debts and incomes. Examiners cannot perform that core function without sufficiently detailed documentation.

Given the Bureau's proposed role for pricing, it is especially important for the lender to retain documentation regarding the pricing decision. Was the pricing indeed reflective of ATR or was it based in impermissible equity-based lending? Was the pricing fair—affordable and responsible—or did it reflect race-based pricing discrimination?

C. Additional consider and verify protections are needed

1. The Bureau should not allow creditors to "mix and match" consider and verify requirements

The Bureau asks if it should allow creditors to "mix and match" consider and verify requirements.[131] Given the undeveloped state of the commentary text on this point ("List to Be Determined"),[132] it is impossible to provide more than a general response to the Bureau's request for comment. Before finalizing the rule, the Bureau should provide all stakeholders with an opportunity to comment on how "mixing and matching" would work with the actual list of documents available for creditors to mix and match.

"Mixing and matching" is almost always a bad practice for any kind of system. The mixing is inarguable; the matching is in the eye of the beholder. The Bureau should not inject unnecessary subjectivity into its standards or it risks having them be no kind of standards at all. At a minimum, the Bureau should limit mixing and matching to circumstances where the differing documents use the same definitions and provide the same standards, so that a creditor is not playing off one set of external standards against another.

2. The Bureau should require consistency in how creditors consider and verify debts and income

If the Bureau, and other agencies, are to do their job in examining creditors for compliance with ATR, the Bureau must ensure that creditors develop and maintain consistent, documented protocols for how debts and income are considered and verified. Anything else permits consider and verify requirements to exist in name only, as individual loan officers make individual decisions about what counts as adequate consideration or verification.

Our experience during the last crisis was not primarily that lenders failed to consider and verify income. We represented clients who had documented income in their loan files. And

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[131] 85 Fed. Reg. 41716, 41754.
[132] 85 Fed. Reg. 41716, 41775.

the lender noted that income, suggesting some sort of consideration. But the income was plainly insufficient to support even a subsistence level after payment of the mortgage, leaving residual income in the low hundreds of dollars for a family of four, for example. Where discretion is unconstrained, loan officers under pressure to make loans can easily make a pro forma note of consideration or create as verification documents lacking credibility, leaving borrowers unprotected by any good faith and reasonable determination of ATR.

VII. Conclusion

Nowhere in the 78 pages of Federal Register text making up the Bureau's General QM definition proposal does the Bureau grapple with the fundamental challenge posed by Dodd-Frank to the Bureau: ensuring the supply of responsible, affordable mortgage credit. This language is a mandate to the Bureau to make sure that credit that is extended is both affordable and responsible; it does not authorize a balancing test.[133] Although the Bureau repeats those words,[134] it does not examine what is meant by either "responsible" or "affordable" or demonstrate how its proposal would ensure that credit provided was either. At best, the Bureau, without sufficient evidentiary support, substitutes default risk for "affordable." Nowhere does the Bureau engage with what is meant by "responsible" mortgage credit.

The original QM rulemaking was started by the Federal Reserve Board with an NPRM in April 2011; the Bureau's assessment notes that rulemaking adjusting the definition continued until March 2016.[135] By contrast, the present proposal was published in the Federal Register in July, with a sixty-day comment period, overlapping with two other proposals also touching on QM. Requests to the Bureau for extensions of time, citing the complexity of the issues and the limited ability of stakeholders to engage fully on short time frames during a pandemic that has impacted every aspect of daily life, have been denied.[136] As we have discussed above, various aspects of the current proposal are not sufficiently developed to allow proper evaluation of the proposal, even had the Bureau granted a more appropriate comment period. Yet, we have nonetheless identified in this comment several areas warranting further research and more rigorous analysis by the Bureau.

The Bureau's announced determination to finish this rulemaking in an abbreviated fashion, coupled with its early and consistent signaling of a unitary plan for revising the QM

[133] The Bureau seems to assert that the statute's mandate is instead a balancing test between "consumer protection" and "access to credit." *See, e.g.*, 85 Fed. Reg. 41716, 41740 ("[T]his approach would balance the competing consumer protection and access to credit considerations described above."). There is no basis in the statute for concluding that the Bureau is supposed to promote a certain acceptable level of unaffordable, irresponsible lending. The closest to a balancing test the statute comes is the finding in 15 U.S.C. § 1639b(a) that balances regulation against ensuring access to "responsible, affordable mortgage credit." Only if the credit is both responsible and affordable is access to it weighed against consumer protection.

[134] "Responsible" is used 37 times in the Bureau's proposal; "affordable" or "unaffordable" are used 52 times in the proposal, and "access to credit" is repeated 78 times in the proposal, once per page of Federal Register text, on average.

[135] Bureau of Consumer Fin. Prot., Ability-to-Repay and Qualified Mortgage Rule Assessment Report, at 18 (Jan. 2019), https://files.consumerfinance.gov/f/documents/cfpb_ability-to-repay-qualified-mortgage_assessment-report.pdf.

[136] August 26, 2020 Letter from Director Kathleen L. Kraninger to Alys Cohen, National Consumer Law Center.

definition, has impeded full consideration of the issues under discussion. The compressed time period, the relative underdevelopment of the Bureau's proposal and its evidentiary basis, and the Bureau's failure to consider reasonable alternatives have hampered our efforts to provide comment. We do not know the extent to which others have also been discouraged from full engagement.

This proposal falls short of a reasoned explanation based in either the statutory language or the data considered. Nor does this proposal reflect a careful weighing of all available alternatives. The Bureau should stop this rulemaking and extend the GSE patch while it conducts the foundational research necessary to answer the difficult and essential questions about how to ensure access to affordable and responsible mortgage credit for all consumers. Such research must consider not only the Bureau's deregulatory tools and the definition of QM but also the role of fair lending enforcement in promoting access to responsible, affordable mortgage credit.

We thank you for the opportunity to submit these comments.

Attachment A

September 8, 2020

The Honorable Kathleen L. Kraninger
Bureau of Consumer Financial Protection
1700 G Street, NW
Washington, DC 20552

RE: Qualified Mortgage Definition under the Truth in Lending Act (Regulation Z): General QM Loan Definition, Docket No. Docket No. CFPB-2020-0020, RIN 3170-AA98

Dear Director Kraninger:

On behalf of the clients and communities we represent, the undersigned organizations respectfully submit the attached term sheet. The term sheet identifies fair lending and "consider and verify" provisions we agree should be included in any modified Qualified Mortgage rule. We urge the Bureau to incorporate these provisions into any final rulemaking, whether by regulation or official interpretation.

Each of the undersigned organizations believes that a meaningful consider and verify requirement in the CFPB's final rule is of critical importance to ensuring that a revised QM definition remains faithful to the ability-to-repay framework that Dodd-Frank created. Thank you for your consideration of our comments.

Sincerely,

Americans for Financial Reform Education Fund
Center for Responsible Lending
Consumer Federation of America
NAACP
NAACP Legal Defense and Educational Fund, Inc. (LDF)
National CAPACD
National Community Stabilization Trust
National Consumer Law Center (on behalf of its low-income clients)
National Community Reinvestment Coalition (NCRC)
National Fair Housing Alliance
National Urban League
UnidosUS

Joint Civil Rights-Consumer Groups Term Sheet on Fair Lending and Consider and Verify Requirements for QM

September 8, 2020

Fair Lending Proposal:

- **No presumption or inferences relating to fair lending**: The CFPB has a separate, yet equally important, responsibility to ensure that the pricing consumers receive for mortgages does not discriminate against applicants on the basis of characteristics protected by law. By statute, one of the functions of the Office of Fair Lending and Equal Opportunity is to coordinate the fair lending efforts of the Bureau with other Federal agencies and State regulators "to promote consistent, efficient, and effective enforcement of Federal fair lending laws." Accordingly, the CFPB should make clear that the QM safe harbor established by this regulation should not be construed to create an inference or presumption that a loan satisfying the identified criteria is compliant with the Equal Credit Opportunity Act, the Fair Housing Act, or state or local anti-discrimination laws that pertain to lending. A QM safe harbor loan may still violate the requirements of the Equal Credit Opportunity Act, the Fair Housing Act or state and local anti-discrimination laws, as well as other federal and state laws regulating mortgage lending.

- **Diminishing negative impacts on a borrower's Ability to Repay**: The CFPB has an obligation to mitigate actions, like pricing discrimination, that can negatively impact a borrower's ability to repay their debt obligation. The CFPB should therefore limit the ability of a financial institution to receive the QM safe harbor in instances where pricing discrimination has occurred, as set forth below.

  If a financial institution, or creditor as defined by the Equal Credit Opportunity Act (ECOA), originates a loan that meets the Safe Harbor thresholds outlined in the regulation and discovers a likely violation of the ECOA resulting from pricing discrimination related to the loan, the financial institution shall self-report the likely violation to the CFPB and its prudential regulator within 30 days of the discovery of the likely violation. The financial institution shall have 30 days, from the date of discovery, to remediate the harm resulting from the likely violation.

  Should a financial institution fail to self-report a likely violation and remediate the harm resulting from a likely violation within 30 days of the date of discovery of the likely violation, and a judicial, administrative, or regulatory body, through a final adjudication, determines that pricing discrimination in violation of ECOA has occurred, the Safe Harbor will not apply to the loan(s) related to that violation. Loans related to that violation may still qualify as QM loans, but they are not afforded a conclusive presumption of compliance.

Consider and Verify:

- **Early defaults**: Creditors should be required to track early defaults and maintain records showing this tracking and any responses to increases in early defaults to ensure link between pricing and ATR.
- **Reasonable and good faith determination**: CFPB should affirm that creditors making QM loans must nonetheless comply with the underlying statutory requirement to make a reasonable and good faith determination of ATR.
    - Consistent with CFPB's request for examples of what "not meaningfully consider" means, outer bounds of what could be consider and verify documentation inconsistent with a reasonable and good faith interpretation of ATR:
        - 100% DTI loans, including 100% at maximum loan payment on current income, and including full DTI for all known debts, including simultaneous loans;
        - Zero or negative residual income (after-tax monthly income less debt payments), after accounting for all known debt obligations, including simultaneous loans;
        - Documentation that is falsified or subject of fraud by or with the knowledge and consent of the lender, broker, or their agents;
        - Statements by borrower that they cannot pay projected payments or can only pay the minimum ARM payment, as reflected in the underwriting file;
        - Promises by lender, broker, or their agents that the lender will refinance the loan upon any stated future event (e.g., ARM reset, financial difficulty experienced by borrower, borrower's retirement), as reflected in the underwriting file;
        - If ARMs are not excluded from QM, CFPB should state that consider and verify, like ATR, has to be based on the maximum payment in the first five years;
        - Escrow requirements must, per the statute, reflect all applicable taxes, insurance, and assessments, including any known post-closing upward adjustments reflecting a new assessment/ loss of exemptions, etc.; and
        - Statements by borrower or other documented evidence that the borrower expects a reduction of income soon unless the underwriting is done in accordance with borrower's projected income drop, as reflected in the underwriting file.

- **Record retention**: At a minimum, the creditor's record retention of how it considered and verified income or assets and DTI or residual income must meet the following standards:
    - As CFPB says, the creditor must verify anything it considers;
    - There must be detailed enough record retention that an examiner could review the underwriting to confirm that it was done in accordance with the creditor's procedures, based on verified information, and that DTI or residual income were considered;
    - The considerations for pricing and an explanation for the pricing must be maintained, including any role played by LTV or equity in the home. Examiners should be able to determine and verify from reviewing the retained documentation the basis of the pricing decision, any applicable weight given to various factors in the consideration (including minimally which factors played a role in determining pricing), and, if present, any mathematical relationships. For example, a printout from the underwriting system saying the loan is approved by itself should be inadequate to demonstrate pricing considerations, if the printout only indicates that the loan was approved and not how it was priced.
    - On any individual loan, to the extent discretionary pricing was permitted and occurred, including any deviations from rate sheets, both any rate sheets used and explanations for deviations from those rate sheets or other discretionary pricing must be retained.
    - To combat the risk of discriminatory pricing, any fair lending analysis conducted on pricing or loans originated must be retained and available for supervisory examinations on QM compliance.
    - In order to maintain the safe harbor against a borrower raising the ATR as a defense to foreclosure, documentation must be retained. If the documentation is not maintained, the creditor or assignee loses the presumption that a good faith determination of ATR was conducted.
- **No asset-based lending**: CFPB should affirm prior interagency guidance that lending on LTV/asset value alone is per se predatory and cannot satisfy the requirements of consider and verify.