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The Exception that Ate the Rule: Why QRM Should Not Equal QM

I. INTRODUCTION

Representative Barney Frank stated that the credit risk retention rule of his namesake legislation, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), was the “single most important part of th[e] bill.”¹ The credit risk retention rule requires securitizers of asset-backed securities (ABS) to hold 5% of the credit risk on any asset they securitize as “skin in the game.”² Congress believed that having skin in the game would align the interests of securitizers with investors and promote a safer secondary market, thus preventing a repeat of the 2008 financial crisis.³ The Dodd-Frank Act provided securitizers of residential mortgage-backed securities (RMBS) an exemption from the credit risk retention requirement if a mortgage met the standards of a “qualified residential mortgage” (QRM).⁴ Congress intended QRMs to mirror mortgages made with certain traits that might have accounted for their historical record of good performance.⁵

In an effort to curb predatory mortgage lending, Congress delineated general mortgage standards within the Dodd-Frank Act which required the lender to establish that the borrower had the ability to repay the loan.⁶ Under these new standards the lender would extend credit based on the borrower’s ability to repay the loan rather than on

1. Shirley Gao, *Dodd-Frank author is proudest of “skin in the game” requirement for mortgage securitizers*, THE CENTER FOR PUBLIC INTEGRITY (Nov. 28, 2011, 11:04 AM), <http://www.publicintegrity.org/2011/07/11/5194/dodd-frank-author-proudest-skin-game-requirement-mortgage-securitizers>.

2. See Investor Protection and Securities Reform Act of 2010, 15 U.S.C. § 78o-11(c)(1)(B) (2012).

3. See S. REP. NO. 111-176, at 129 (2010).

4. 15 U.S.C. § 78o-11(e)(4).

5. See generally 156 CONG. REC. S3575 (daily ed. May 12, 2010) (statement of Sen. Mary Landrieu) (discussing how QRM should be defined).

6. See Mortgage Reform and Anti-Predatory Lending Act, 15 U.S.C. § 1639c (2012).

the pre-closure value of the home securing the loan.⁷ The ability-to-repay rule was created to maintain a broad availability of credit to consumers while ensuring that lenders were selling safe products.⁸ The ability-to-repay rule exposed mortgage originators to substantial liability if the originator did not make a reasonable and good-faith determination based on verified and documented information that the consumer had a reasonable ability to repay the loan at the time the loan was consummated.⁹ The rule provides a safe harbor and rebuttable presumption of compliance.¹⁰ The lender need not establish the borrower's ability to repay if the loan is a "qualified mortgage" (QM).¹¹ The QM standard was intended to be a general mortgage underwriting standard that captured a majority of the traditional mortgage market to prevent restriction of credit availability.¹²

Congress instructed the newly created Consumer Financial Protection Bureau (CFPB) to define QM and instructed six federal agencies, the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, the Secretary of Housing and Urban Development, and the Director of the Federal Housing Finance Agency (collectively "the Agencies"), to jointly define QRM.¹³ In April 2011, the Agencies proposed a definition of QRM that received considerable negative feedback.¹⁴ The CFPB did not release its final definition of QM until January 2013.¹⁵ Due to the negative feedback on the proposed QRM definition, the Agencies re-proposed the QRM definition in August 2013 aligning the

7. *Id.*

8. See generally Raymond Natter, *Congressional Intent Regarding the Qualified Mortgage Provision*, SELECTEDWORKS available at http://works.bepress.com/raymond_natter/2/ (discussing Congress's intent in creating the ability-to-repay rule).

9. See 15 U.S.C. § 1639c(a)(1).

10. *Id.* § 1639c(b).

11. *Id.*

12. See Natter, *supra* note 8, at 9-12.

13. 15 U.S.C. § 1639c(b)(3)(B); 15 U.S.C. 78o-11(b)(2).

14. See Credit Risk Retention, 76 Fed. Reg. 24,090, 24,120 (proposed Apr. 29, 2011) (to be codified at 12 C.F.R. pt. 43); Credit Risk Retention, 78 Fed. Reg. 57,928, 57,988 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43).

15. Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6408 (Jan. 30, 2013) (to be codified at 12 C.F.R. pt. 1026).

meaning of QRM with the CFPB's definition of QM.¹⁶ However, because the Agencies (which ironically does not include the CFPB) continue to disagree on which definition to adopt for QRM, they also included an alternative to the QRM-QM definition called QM-Plus.¹⁷

This Note discusses why Congress did not intend for QRM to mean QM as defined by the CFPB and, therefore, why the re-proposed rule should not be adopted. Part II provides a brief background of the financial crisis.¹⁸ Part III discusses the ability-to-repay and credit risk retention rules under the Dodd-Frank Act.¹⁹ Part IV then examines the CFPB's and the Agencies' rulemaking that define QM and QRM.²⁰ Finally, in Part V, this Note concludes that QRM should not have the same meaning as QM because Congress intended to protect two distinct groups, each needing a separate definition tailored to its specific goals.²¹

II. THE FINANCIAL CRISIS

In 2008, the United States entered into the worst financial crisis it has seen since the Great Depression.²² Rising home prices and significant decreases in interest rates created a housing bubble in the early 2000s.²³ Nontraditional mortgage products were created in part to help borrowers afford to buy a home in this housing market.²⁴ In some cases, these mortgages were deceptive.²⁵ When low teaser rates expired and reset at higher rates, borrowers were often able to avoid the increased payments by refinancing to a new nontraditional mortgage

16. Credit Risk Retention, 78 Fed. Reg. at 57,989.

17. *Id.* at 57,993.

18. *See infra* Part II.

19. *See infra* Part III.

20. *See infra* Part IV.

21. *See infra* Part V.

22. *See* Thomas F. Siems, *Branding the Great Recession*, FIN. INSIGHTS (FED. RESERVE BANK OF DALL.) May 13, 2012, at 3, available at <http://www.dallasfed.org/assets/documents/banking/firm/fi/fi1201.pdf> (discussing why the 2008 financial crisis is the worst financial crisis since the Great Depression).

23. Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6408, 6410 (Jan. 30, 2013) (to be codified at 12 C.F.R. pt. 1026).

24. *See* Bill Thomas, Keith Hennessey & Douglas Holtz-Eakin, *What Caused the Financial Crisis*, WALL ST. J., Jan. 27, 2011, <http://online.wsj.com/article/SB10001424052748704698004576104500524998280.html> (giving one opinion on what caused the financial crisis).

25. *Id.*

with a new low teaser interest rate.²⁶ Lenders exacerbated the problem by permitting borrowers to sign up for so-called “low documentation” or “no documentation” loans, which often “featured loan applications characterized by misstated or falsified income.”²⁷ When the housing bubble burst and home prices dropped, borrowers facing interest rate resets lost the ability to refinance their mortgages or were unwilling to make payments because the value of their homes declined below the amount they owed on their mortgages.²⁸ This led to many borrowers defaulting on their nontraditional mortgage loans.²⁹

Failures in credit rating and securitization transformed these mortgages into toxic financial assets, of which large and midsize financial institutions amassed enormous concentrations.³⁰ Financial institutions failed to grasp the risk they were taking on because they neglected to look behind the ratings and do their own due diligence.³¹ By the early 2000s, many private financial institutions were using securities and derivative products to create complex mortgage-related investment vehicles.³² The risk associated with these products was amplified by financial institutions holding too little capital relative to the risks they were amassing.³³ When the housing bubble burst and defaults increased, the mortgage-backed asset class also collapsed resulting in a cascade of firm failures, mergers, and restructurings which caused financial shock and panic.³⁴ Trust and confidence in the U.S. financial system washed away, as the health of almost all large and midsize financial institutions was questioned, causing a severe contraction in the real economy.³⁵

26. See Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. at 6410.

27. H.R. REP. NO. 111-94, at 163 (2009).

28. See Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. at 6410.

29. See Josh Clark, *How can mortgage-backed securities bring down the U.S. economy?*, HOWSTUFFWORKS, <http://money.howstuffworks.com/mortgage-backed-security2.htm> (last visited Nov. 4, 2013).

30. Thomas, Hennessey & Holtz-Eakin, *supra* note 24.

31. See Clark, *supra* note 29.

32. Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. at 6411.

33. Thomas, Hennessey & Holtz-Eakin, *supra* note 24.

34. *Id.*

35. *Id.*

III. ABILITY-TO-REPAY AND RISK RETENTION UNDER THE DODD-FRANK ACT

The United States initially responded to the financial crisis by buying preferred stock in many of the largest financial institutions that were deemed “too big to fail” through the Troubled Asset Relief Program (TARP).³⁶ The government also investigated the root causes of the financial crisis and began to draft legislation to correct the underlying issues.³⁷ Two years after the 2008 financial crisis, Congress passed the Dodd-Frank Act to restore accountability and consumer confidence in the financial system.³⁸ To combat the underlying mortgage issues, the Dodd-Frank Act changed numerous federal laws that regulate mortgage practices with the aim of ending predatory lending practices and providing certain protections to borrowers and investors.³⁹

A. *Creation of the Consumer Financial Protection Bureau*

Congress recognized that there was a failure of the federal banking agencies and other regulators to address significant consumer protection issues.⁴⁰ These failures were harmful to both consumers and the banking system.⁴¹ Congress concluded that the current system of consumer protection suffered from a number of fundamental flaws that undercut its effectiveness, “including a lack of focus resulting from conflicting regulatory missions, fragmentation, and regulatory arbitrage.”⁴² The banking agencies’ primary mission was to ensure the safe and sound operations of the banks rather than to protect consumers,

36. See Jesse Nankin & Krista K. Schmidt, *History of U.S. Gov’t Bailouts*, PROPUBLICA, <http://www.propublica.org/special/government-bailouts> (last updated Apr. 15, 2009).

37. See generally Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), Pub. L. No. 111-203, 124 Stat. 1376 (2010).

38. S. COMM. ON BANKING, HOUSING, & URBAN AFFAIRS, 111TH CONG., BRIEF SUMMARY OF THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT, *available at* http://www.banking.senate.gov/public/_files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf.

39. H.R. REP. NO. 110-441, at 50-51 (2007).

40. S. REP. NO. 111-176, at 9 (2010).

41. *Id.*

42. *Id.* at 10.

putting consumer protection in competition with regulatory goals.⁴³ The Federal Reserve Board had the main responsibility for federal mortgage lending rules, and it did not act with a regulation regarding mortgage practices until 2008⁴⁴—far too late in the game. Furthermore, at that time, there were seven agencies involved in consumer rule writing or enforcement, leading to fragmentation, which undermined accountability and caused regulatory arbitrage between federal regulators and the states.⁴⁵

The Dodd-Frank Act remedied these structural flaws and sought to protect consumers by creating the Bureau of Consumer Financial Protection (now commonly referred to as the Consumer Financial Protection Bureau or CFPB), which regulates how financial products or services are offered and provided to consumers under federal law.⁴⁶ Responsibility for the existing federal consumer protection statutes and regulations, including the Truth in Lending Act (TILA), were transferred from the Federal Reserve Board to the CFPB.⁴⁷ With the CFPB's new rulemaking power, it amended TILA to implement § 1411⁴⁸ and § 1412⁴⁹ of the Dodd-Frank Act.⁵⁰

B. *Ability to Repay*

The Dodd-Frank Act amended TILA to include the ability-to-repay requirement.⁵¹ The CFPB alone was charged with defining the ability-to-repay standard, providing minimum underwriting standards for mortgages.⁵² The ability-to-repay rule imposed liability on residential mortgage lenders if they did not make a reasonable and

43. *Id.*

44. *See* Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6408, 6408 (Jan. 30, 2013) (to be codified at 12 C.F.R. pt. 1026).

45. S. REP. NO. 111-176, at 10.

46. Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), 12 U.S.C. § 5491 (2012).

47. *See Id.* § 5481(12)(O), 5581(b)(1).

48. Implementing ability-to-repay. *See* Mortgage Reform and Anti-Predatory Lending Act, 15 U.S.C. § 1639c(a) (2012).

49. Implementing the rebuttable presumption and safe harbor. *See* 15 U.S.C. § 1639a(d).

50. Truth in Lending (Regulation Z), 12 C.F.R. § 1026 (2013).

51. *See* 15 U.S.C. § 1639c (Ability to repay under TILA).

52. *Id.*; *see also* H.R. REP. NO. 111-94, at 48 (2009).

good-faith determination based on verified and documented information that the consumer had a reasonable ability to repay the loan.⁵³ Under this rule, mortgage providers would be required to lend to consumers who have a reasonable ability to repay the mortgage at the time of origination.⁵⁴ The Dodd-Frank Act created a safe harbor and a rebuttable presumption against ability-to-repay liability when creditors made Qualified Mortgages.⁵⁵ The CFPB released its final rule for the ability-to-repay requirement and safe harbor, defining QM, in January 2013 which became effective on January 10, 2014.⁵⁶

C. *Risk Retention Requirement – Keeping “Skin in the Game”*

The Dodd-Frank Act also provides protection to investors of ABS.⁵⁷ It requires securitizers to retain a material amount of risk, causing them to have “skin in the game” by aligning the securitizers’ economic interests with those of investors in the ABS.⁵⁸ These protections are intended to reform mortgage lending practices to prevent a recurrence of rising defaults and foreclosures and to protect investors who purchase assets backed by such mortgages.⁵⁹

Although Congress adopted the credit risk retention rule which requires any securitizer of ABS to retain at least 5% of the securities risk,⁶⁰ it also provided an exception to the credit risk retention rule for mortgage-backed securities (MBS) if the securitized mortgages were Qualified Residential Mortgages.⁶¹ The Dodd-Frank Act requires that the Agencies, not including the CFPB, jointly define QRM.⁶² The Dodd-Frank Act also stipulated that the definition of QRM could not be broader than the definition of QM, as defined under § 129C(c)(2) of

53. 15 U.S.C. § 1639c(a)(1).

54. *Id.* § 1639b(c)(3).

55. *Id.* § 1639c(b).

56. Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6408, 6408 (Jan. 30, 2013) (to be codified at 12 C.F.R. pt. 1026).

57. Mortgage Reform and Anti-Predatory Lending Act, 15 U.S.C. 78o-11 (2012); *see also* S. REP. NO. 111-176, at 129 (2010).

58. 15 U.S.C. § 78o-11.

59. H.R. REP. NO. 110-441, at 49 (2007).

60. 15 U.S.C. § 78o-11(c)(1)(B)(i).

61. *Id.* § 78o-11(e)(4) (2012).

62. *Id.* § 78o-11(e)(4)(A).

TILA, as amended by the CFPB.⁶³

IV. RULEMAKING BY THE CFPB AND THE AGENCIES DEFINING QM AND QRM

A. *The Agencies' First Proposed Qualified Residential Mortgage Definition*⁶⁴

The Agencies jointly released a proposed credit risk retention rule that defined QRM on April 29, 2011.⁶⁵ The proposed risk retention rule would have applied to securitizers of ABS⁶⁶ and required such securitizers to retain not less than 5% of the credit risk⁶⁷ for any asset that the securitizer transferred, sold, or conveyed to a third party, “unless an exemption from the risk retention rules for the securities or transaction was otherwise available.”⁶⁸ One exemption available to securitizers stated that the risk retention rules would not apply to an

63. *Id.* § 78o-11(e)(4)(C).

64. *See infra* Appendix (side-by-side comparison of the key differences between the original QRM proposal and the final QM definition).

65. *See* Credit Risk Retention, 76 Fed. Reg. 24,090 (proposed Apr. 29, 2011) (to be codified at 12 C.F.R. pt. 43).

66. 15 U.S.C. § 78c(a)(77) (defining an ABS as “a fixed-income or other security collateralized by any type of self-liquidating financial asset (including a loan, a lease, a mortgage, or a secured or unsecured receivable) that allows the holder of the security to receive payments that depend primarily on cash flow from the asset, including—(i) a collateralized mortgage obligation; (ii) a collateralized debt obligation; (iii) a collateralized bond obligation; (iv) a collateralized debt obligation of asset-backed securities; (v) a collateralized debt obligation of collateralized debt obligations; and (vi) a security that the Commission, by rule, determines to be an asset-backed security for purposes of this section; and (B) does not include a security issued by a finance subsidiary held by the parent company or a company controlled by the parent company, if none of the securities issued by the finance subsidiary are held by an entity that is not controlled by the parent company.”).

67. The re-proposed credit risk retention rule allows sponsors to hold credit risk as an “eligible vertical interest,” an “eligible horizontal residual interest,” or any combination thereof, in a total amount equal to no less than 5% of the fair value of all ABS interests in the issuing entity that are issued as part of the securitization transaction. Under the vertical risk retention option, a sponsor could satisfy its risk retention requirement by retaining at least 5% of each class of ABS interests issued as part of the securitization transaction. Under the horizontal risk retention option, a sponsor could satisfy its risk retention obligations by retaining a first-loss “eligible horizontal residual interest” in the issuing entity in an amount equal to at least 5% of the par value of all ABS interests in the issuing entity that were issued as part of the securitization transaction. Credit Risk Retention, 78 Fed. Reg. 57,928, 57,936-57,937 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43).

68. Credit Risk Retention, 76 Fed. Reg. at 24,099.

issuance of ABS if all of the assets that collateralized the ABS were Qualified Residential Mortgages.⁶⁹

Initially, the Agencies defined QRM to mean any mortgage that was a closed-end, first-lien mortgage to purchase or refinance a one-to-four family property with at least one unit being the principal dwelling of the borrower.⁷⁰ The borrower could not have certain “derogatory factors” for the mortgage to be considered a QRM.⁷¹ For instance, borrowers could not be past due, in whole or in part, on any debt obligation within two years and could not have been engaged in certain activities such as bankruptcy within a specified amount of time.⁷² Mortgage originators would have to verify and document compliance with these factors within ninety days prior to closing.⁷³

A QRM could not include payment terms that allowed for interest-only payments, negative amortization, balloon payments,⁷⁴ or prepayment penalties.⁷⁵ For any adjustable-rate mortgages (ARM), the proposal set maximum rate increases for the life of the mortgage.⁷⁶ Under the proposed rule, a QRM had to have a loan-to-value (LTV) ratio of 80% or less for purchase-money mortgage transactions, 75% or less on rate and term refinance loans, and 70% or less for cash-out refinance loans.⁷⁷ Thus, for a purchase-money mortgage, a down payment of at least 20% of the home’s purchase price was required,

69. *Id.* at 24,117.

70. *Id.* at 24,166.

71. *Id.*; *see also id.* at 24,121.

72. *Id.* at 24,121-22, 24,166 (a borrower must not currently be thirty or more days past due, in whole or in part, on any debt obligation, and the borrower must not be sixty or more days past due, in whole or in part, on any debt obligation within the preceding twenty-four months. A borrower must not have, within the preceding thirty-six months, been a debtor in a bankruptcy proceeding, had property repossessed or foreclosed upon, engaged in a short sale or deed-in-lieu of foreclosure, or been subject to a federal or state judgment for collection of any unpaid debt).

73. *Id.* at 24,122, 24,166.

74. 12 C.F.R. § 226.18(s)(5)(i) (2013) (defining “balloon payment” as “any scheduled payment of principal and interest that is more than twice as large as any earlier scheduled payment of principal and interest”).

75. Credit Risk Retention, 76 Fed. Reg. at 24,122, 24,166 (“A prepayment penalty is defined as a penalty imposed solely because the mortgage obligation is prepaid in full or in part. For purposes of this definition, a prepayment penalty would not include, for example, fees imposed for preparing and providing documents in connection with prepayment, such as a loan payoff statement, a reconveyance, or other document releasing the creditor’s security interest in the one-to-four family property securing the loan.”).

76. *Id.*

77. *Id.* at 24,123, 24,167.

with a higher equity requirement for refinancing.⁷⁸

The first proposal required a QRM to have a qualifying written appraisal, which conformed to generally accepted appraisal standards.⁷⁹ Additionally, the QRM proposal required two debt-to-income (DTI) ratios, one which compared the borrower's monthly mortgage payment with his monthly gross income (front-end ratio), and another that compared the borrower's monthly total debts with his monthly gross income (back-end ratio).⁸⁰ The proposal limited QRMs to mortgages that had a front-end ratio of 28% and a back-end ratio of 36%.⁸¹

Under the first proposal, a QRM could not be assumed by any person who was not a borrower under the original mortgage transaction.⁸² Someone who assumes a mortgage may not meet the QRM standards, changing the risk associated with the securitized mortgage, which could have negative effects on the investor.⁸³ A QRM under the original proposal also required the originator of a QRM to incorporate certain requirements regarding servicing policies and procedures for the mortgage into the mortgage transaction documents.⁸⁴

B. *The CFPB's Proposed and Final Qualified Mortgage Definition*

1. The Proposed Qualified Mortgage Definition

On May 11, 2011, the Board of Governors of the Federal Reserve System (the "Board") published a proposed rule amending TILA to include the ability-to-repay requirement and the safe harbor and rebuttable presumption provisions, which defined QM.⁸⁵ The

78. *See id.* at 24,124, 24,167.

79. *Id.* at 24,125, 24,167 (Generally accepted appraisal standards are evidenced by the Uniform Standards of Professional Appraisal Practice, the appraisal requirements of the federal banking agencies, and applicable laws).

80. *Id.* at 24,125, 24,166.

81. Credit Risk Retention, 76 Fed. Reg. at 24,125, 24,166.

82. *Id.* at 24,126-27, 24,167.

83. *Id.* at 24,126-27.

84. *Id.* at 24,127, 24,167 (servicing policies and procedures included information regarding loss mitigation actions, subordinate liens, and the responsibility for assumption of these requirements if the servicing rights with respect to the QRM were sold or transferred to another business entity).

85. Regulation Z; Truth in Lending, 76 Fed. Reg. 27,390 (proposed May 11, 2011) (to be codified at 12 C.F.R. pt. 226).

proposal mentioned other recent actions that the Board had been involved with including its joint effort, as a member of the Agencies, to implement the credit risk retention rule which defines QRM.⁸⁶ The proposed rule acknowledged that the Agencies defined QRM by taking into consideration underwriting and product features that historical loan-performance data indicated resulted in a lower risk of default and that QRM could be no broader than the definition of a QM under TILA.⁸⁷ QRM was not discussed any further in the Board's proposal defining QM.⁸⁸

The proposal included two alternative definitions for QM because the Board was concerned with ambiguity surrounding whether QM created a safe harbor or a rebuttable presumption.⁸⁹ The first alternative defined a QM based on the criteria listed in the Dodd-Frank Act and operated as a legal safe harbor and alternative to complying with the general ability-to-repay standard.⁹⁰ It did not include a requirement to consider the consumer's DTI ratio or residual income.⁹¹ The second alternative defined a QM to include the requirements listed in the Dodd-Frank Act as well as other underwriting requirements that are in the general ability-to-repay standard such as employment status, simultaneous loans, current debt obligations, DTI ratio, and credit history.⁹² This alternative provided a presumption of compliance that could be rebutted by the consumer.⁹³

Although the Board actively participated in defining both QM and QRM, the two definitions differed greatly.⁹⁴ Neither QM alternative included a down payment requirement, LTV ratio requirement, any written appraisal requirement, any assumability requirement, or any servicing standards.⁹⁵ Furthermore, only one alternative required a QM to consider a borrower's DTI ratio, which did

86. *Id.* at 27,393-94.

87. *Id.* at 27,394.

88. *See id.* at 27,390-506.

89. *Id.* at 27,396, 27,484-85.

90. *Id.* at 27,396, 27,484.

91. Regulation Z; Truth in Lending, 76 Fed. Reg. at 27,396, 27,484.

92. *Id.* at 27,396, 27,484-85.

93. *Id.*

94. *See id.*; Credit Risk Retention, 76 Fed. Reg. 24,122, 24,166-67 (proposed Apr. 29, 2011) (to be codified at 12 C.F.R. pt. 43) (criteria for QRM exemption).

95. *See* Regulation Z; Truth in Lending, 76 Fed. Reg. at 27,396, 27,484-85.

not give a quantitative standard,⁹⁶ and only one alternative considered standards related to a borrower's credit history.⁹⁷ The Board requested comments on both QM alternatives while the Agencies also sought comments on the QRM definition released two weeks earlier.⁹⁸

2. The CFPB's Final Qualified Mortgage Definition

Effective July 21, 2011, the Dodd-Frank Act transferred the Board's rulemaking authority for TILA to the CFPB.⁹⁹ On January 30, 2013, the CFPB published a final rule amending TILA to include the ability-to-repay requirement and a safe harbor and rebuttable presumption, which defined QM.¹⁰⁰ The CFPB's final QM rule provides a safe harbor and presumption of compliance with the ability-to-repay requirement for mortgages that are not high-priced loans and a rebuttable presumption for mortgages considered high-priced loans.¹⁰¹ The CFPB's final rule recognized the continued fragility of the mortgage market and the effects that its definition of QM could have on other rulemaking under the Dodd-Frank Act, such as defining QRM.¹⁰²

The CFPB explained that the credit risk retention requirement, defining QRM, was "aimed at addressing weaknesses and failures in the securitization process and the securitization markets."¹⁰³ The rule noted that the Agencies, not including the CFPB, were tasked with implementing the credit risk retention requirement.¹⁰⁴ The final rule included the Agencies' proposed QRM definition and stated that the CFPB worked with the Agencies so that QRM would be no broader

96. The Board did not want to set a quantitative standard for DTI because it feared it could limit credit availability without providing adequate off-setting benefits. *Id.* at 27,460.

97. *Id.* at 27,396.

98. *See id.*; Credit Risk Retention, 76 Fed. Reg. at 24,122.

99. Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 6408, 6418 (Jan. 30, 2013) (to be codified at 12 C.F.R. pt. 1026).

100. *See id.* at 6408.

101. 12 C.F.R. § 1026.43(e).

102. Ability-to-Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. at 6412.

103. *Id.* at 6416.

104. *Id.*

than QM as mandated by the Dodd-Frank Act.¹⁰⁵ Although both QM and QRM are designed to address problems that arose in the mortgage-origination process, the CFPB noted that the QM and QRM definitions are “distinct and relate[d] to different parts of the Dodd-Frank Act with different purposes.”¹⁰⁶ Furthermore, the final rule stated that while the CFPB’s QM definition set the outer limits of a QRM, the Agencies had the option under the Dodd-Frank Act to define QRM in a way that was narrower than the QM definition.¹⁰⁷

Unlike the QRM proposal which had only one QRM definition for all applicable mortgages, the CFPB’s final ability-to-repay rule provided multiple definitions for QM.¹⁰⁸ The QM definitions fell into three main categories: general QMs, Government-Sponsored Enterprise (GSE) eligible QMs, and small-creditor QMs.¹⁰⁹ In general, a QM is any consumer credit transaction that is secured by a dwelling,¹¹⁰ including any real property attached to a dwelling except for certain exempt transactions.¹¹¹ A QM is a transaction that provides for regular periodic payments that are substantially equal (except for adjustable-rate or step-rate mortgages) that do not increase the principal balance, allow deferred repayment of principal, or create a balloon payment with some exceptions.¹¹² A QM cannot have a loan term that exceeds thirty years or have total points and fees payable in connection

105. *Id.* at 6417.

106. *Id.*

107. *Id.*

108. *Compare* Credit Risk Retention, 76 Fed. Reg. 24,090, 24,117-27 (proposed Apr. 29, 2011) (to be codified at 12 C.F.R. pt. 43), with 12 C.F.R. § 1026.43(e)(2) (QM defined—generally); (e)(4) (QM defined—special rules); (e)(5) (QM defined—small creditor portfolio loans); (e)(6) (QM defined—temporary balloon payments); (f) (balloon payment QM made by certain creditors).

109. *What is a Qualified Mortgage?*, CONSUMER FIN. PROT. BUREAU, http://files.consumerfinance.gov/f/201310_cfpb_qm-guide-for-lenders.pdf (last visited Nov. 6, 2013).

110. “Dwelling means a residential structure that contains one to four units, whether or not that structure is attached to real property. The term includes an individual condominium unit, cooperative unit, mobile home, and trailer, if it is used as a residence.” 12 C.F.R. § 1026.2(a)(19).

111. 12 C.F.R. § 1026.43(a) (exempt transactions). Unlike the original QRM definition, 12 C.F.R. § 1026.43(a) does not require at least one property to be the principle residence of the borrower. *Compare id.*, with Credit Risk Retention, 76 Fed. Reg. at 24,120 (showing that the originally proposed QRM standard required at least one property to be the principle residence of the borrower).

112. 12 C.F.R. § 1026.43(e)(2)(i).

with the loan exceeding certain specified amounts.¹¹³ Furthermore, to be eligible as a QM, the creditor must underwrite the loan accounting for any monthly payments for mortgage-related obligations.¹¹⁴

Under the final QM definition, a creditor must consider and verify at or before the consummation of the loan the “consumer’s current or reasonably expected income or assets other than the value of the dwelling . . . that secures the loan.”¹¹⁵ The final rule also established that the consumer’s monthly DTI ratio cannot exceed 43% at the time the loan is consummated.¹¹⁶ Similar to the Board’s proposed QM definition, the CFPB did not adopt key features from the Agencies proposed QRM definition in any of its final QM definitions such as a down payment requirement, a LTV ratio requirement, a written appraisal requirement, an assumability requirement, or any servicing standards.¹¹⁷

C. *The Agencies Re-Proposed Qualified Residential Mortgage Definition*¹¹⁸

After receiving a substantial amount of negative feedback concerning the first proposed credit risk retention rule, the Agencies jointly released an amended proposed credit risk retention rule that redefined QRM on August 28, 2013.¹¹⁹ Consistent with the original proposal, the re-proposal also applies to securitizers issuing ABS and would require such “securitizer[s] to retain not less than [5%] of the credit risk for any asset that the securitizer, through the issuance of an

113. *Id.* § 1026.43(e)(2)(ii)-(iii); *see also id.* § 1026.43(e)(3) (setting total point and fee limitations).

114. 12 C.F.R. § 1026.43(e)(2)(iv) (using the maximum interest rate that may apply during the first five years after the date on which the first regular periodic payment will be due and the periodic payments of principal and interest that repay the outstanding principal balance using the maximum interest rate or the loan amount over the loan term).

115. *Id.* § 1026.43(e)(2)(v) (the creditor must also consider and verify the consumer’s current debt obligations, alimony, and child support payments).

116. *Id.* § 1026.43(e)(2)(vi).

117. *See* 12 C.F.R. § 1026.43.

118. *See infra* Appendix (side-by-side comparison of the key differences between the original QRM proposal and the final QM definition).

119. *See* Credit Risk Retention, 78 Fed. Reg. 57,928, 57,933 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43); *SEC Proposed Rules*, U.S. SECURITIES AND EXCHANGE COMMISSION, <http://www.sec.gov/rules/proposed.shtml> (last visited Feb. 1, 2014) (showing that the proposed rule was released on August 28, 2013).

ABS, transfers, sells, or conveys to a third party, unless an exemption from the risk retention requirements for the securities or transaction is otherwise available.”¹²⁰

Due to an overwhelming majority of negative comments concerning the original definition of QRM from “individuals, industry participants, (e.g., real estate brokers, mortgage bankers, securitization sponsors), insurance companies, public interest groups, state agencies, financial institutions, and trade organizations,” the Agencies jointly decided to amend the original QRM definition.¹²¹ Most of the negative comments were focused on the original proposal’s down payment requirement, LTV ratios, and DTI ratios.¹²² Many commenters argued that the proposed QRM definition was too narrow, especially with respect to the LTV and DTI requirements, because it disadvantaged first-time homebuyers and low- and moderate-income persons.¹²³ These commenters asserted that the proposed QRM definition would prevent recovery of the housing market by restricting available credit and make it difficult for private capital to compete with GSEs, stifling the return of private capital to the mortgage market.¹²⁴ The Agencies were strongly encouraged by members of Congress to eliminate or modify the down payment requirement because “the proposed 20% down payment requirement was inconsistent with legislative intent.”¹²⁵

In response to the negative comments, the Agencies’ re-proposal broadened and simplified the scope of the original QRM definition by defining QRM to have the same meaning as QM as defined in § 129C of TILA¹²⁶ and implemented by CFPB regulation.¹²⁷ The Agencies recognized that the CFPB provided several definitions for a QM and proposed that a QRM would be a loan that meets any of the QM definitions under TILA.¹²⁸ QRM equating to QM is a major overhaul of the original QRM definition because it excludes any down payment

120. Credit Risk Retention, 78 Fed. Reg. at 57,935.

121. *Id.* at 57,988-89.

122. *See id.* at 57,988.

123. *Id.*

124. *Id.*

125. *Id.*

126. *See* 15 U.S.C. 1639(c).

127. Credit Risk Retention, 78 Fed. Reg. at 57,989.

128. *Id.* at 57,991; *see also* 12 C.F.R. § 1026.43(e)(2), (e)(4), (e)(5), (e)(6), (f) (QM definitions under TILA).

requirement, LTV ratio requirement, standards related to a borrower's credit history, any written appraisal requirement, any assumability requirement, and any servicing standards that were key features of the original QRM definition.¹²⁹

The Agencies stated that they changed the original QRM definition because they believe setting QRM to mean QM meets the statutory goals and directive of the credit risk retention rule under the Securities and Exchange Act of 1934 “to limit credit risk, preserve[] access to affordable credit, and facilitate[] compliance.”¹³⁰ The Agencies believe that the QM standards combined with the general ability-to-repay rules provide a better level of risk¹³¹ to qualify as a QRM by restricting certain product features and lax underwriting practices that contributed significantly to the financial crisis.¹³² They are also worried about imposing further limitations on mortgage credit availability because such limitations could “disproportionately affect groups that have historically been disadvantaged in the mortgage market, such as lower income, minority, or first-time homebuyers.”¹³³ The Agencies noted potential risks that could arise from setting QRM to mean QM but believe them to be smaller than the risks associated with two distinct definitions.¹³⁴

1. Alternative QRM Definition – QM-Plus

Within the re-proposed credit risk retention rule, the Agencies provided an alternative definition to “QRM means QM,” referred to as “QM-plus.”¹³⁵ The QM-plus definition was considered alongside the “QRM means QM” definition.¹³⁶ The Agencies are seeking feedback on QM-plus in addition to the primary “QRM means QM” definition.¹³⁷ The QM-plus definition would take the QM criteria as a starting point

129. *See* Credit Risk Retention, 78 Fed. Reg. at 57,992.

130. *Id.* at 57,989.

131. The agencies show a 23% default rate for QM loans compared to a 44% default rate for non-QM loans. *See id.* at 57,989-90.

132. *Id.* at 57,989-90.

133. *Id.* at 57,991.

134. *See id.* at 57,990-91.

135. Credit Risk Retention, 78 Fed. Reg. at 57,993.

136. *See Id.*

137. *Id.*

for the QRM definition, and then incorporate four additional standards intended to cut down the risk of default.¹³⁸ Consequently, under QM-plus, a large number of loans would not likely qualify as a QRM, and thus would not gain an exemption from the credit risk retention rule.¹³⁹

The most controversial requirement under the QM-plus definition states that a QRM-eligible mortgage cannot have a LTV ratio exceeding 70% at the time of closing.¹⁴⁰ Thus, a QM-plus mortgage must have a minimum down payment of 30% of the purchase price of the home even though a majority of the commenters disliked the original QRM definition for having a 20% down payment requirement.¹⁴¹ Because QM-plus started with the core QM criteria, a QRM would be required to include the QM's requirements for product type, loan term, points and fees, underwriting, income and debt verification, and DTI ratio.¹⁴² Therefore, QM-plus requires the borrower's DTI ratio not to exceed 43% instead of setting limits to a borrower's front-end and back-end DTI ratios as the original QRM definition proposed.¹⁴³

Under QM-plus, mortgages that qualify as QMs because they meet the CFPB's provisions for balloon loan provisions, GSE-eligible covered transactions, or small-creditor exceptions would not be considered QRMs.¹⁴⁴ Like the original QRM proposal, only loans that constituted the principal dwelling of the borrower would qualify as a QRM under the QM-plus definition.¹⁴⁵ Furthermore, under the QM-plus definition, all QRMs would be required to be first-lien mortgages.¹⁴⁶ Also like the original QRM proposal, borrowers cannot have certain derogatory factors under QM-plus in order to qualify as a

138. *Id.*

139. *Id.*

140. *Id.* at 57,994 (In other words, the QM-plus approach would require a 30% down payment.).

141. Credit Risk Retention, 78 Fed. Reg. at 57,994 (30% down payment requirement); Credit Risk Retention, 76 Fed. Reg. 24,090, 24,124 (proposed Apr. 29, 2011) (to be codified at 12 C.F.R. pt. 43) (20% down payment requirement).

142. *See* Credit Risk Retention, 78 Fed. Reg. at 57,993; *see also* 12 C.F.R. § 1026.43(e)(2) (re-proposal's alternative definition to QRM).

143. *See* Credit Risk Retention, 78 Fed. Reg. at 57,993; 12 C.F.R. § 1026.43(e)(2)(vi).

144. Credit Risk Retention, 78 Fed. Reg. at 57,993.

145. *Id.*

146. *Id.*

QRM.¹⁴⁷

The Agencies recognized that a definition that equates QRM with QM covers a significant portion of the historical mortgage market and most of the present mortgage market.¹⁴⁸ QM-plus, like the original QRM proposal, was meant to capture a significantly smaller portion of the mortgage market requiring securitizers to retain risk for QMs that do not meet the additional four factors.¹⁴⁹ Comments on the re-proposed credit risk retention rule, including the definitions of “QRM meaning QM” and QM-plus, had to be submitted by October 30, 2013.¹⁵⁰

V. QRM SHOULD NOT EQUAL QM

Co-sponsor to the Dodd-Frank Act, Representative Barney Frank, stated that the provision requiring mortgage securitizers to keep skin in the game was the “single most important part of [the] bill.”¹⁵¹ The agencies that have been empowered by Congress to create the standards for the credit risk retention rule and define QRM have given too much weight to industry opinion by allowing the definition of QRM to equate to QM as defined under § 129C of TILA.¹⁵² By defining QRM to mean QM, the Agencies have punted their responsibility to require risk retention by creating the broadest definition of QRM possible.¹⁵³ This was not Congress’s intention when it created the credit risk retention rule, the “single most important part of [the] bill,”¹⁵⁴

147. *Id.* at 57,993-94 (requiring the originator to determine that the borrower was not currently thirty or more days past due on any debt obligation and the borrower had not been sixty or more days past due on any debt obligations within the preceding twenty-four months; furthermore, the borrower must not have been a debtor in a bankruptcy proceeding within the preceding thirty-six months or been subject to a judgment for collection of an unpaid debt, had personal property repossessed, had any one-to-four family property foreclosed upon, or engaged in a short sale or deed in lieu of foreclosure).

148. *Id.* at 57,994.

149. *Id.*

150. Credit Risk Retention, 78 Fed. Reg. at 57,928.

151. Gao, *supra* note 1.

152. *See* Credit Risk Retention, 78 Fed. Reg. at 57,989.

153. *See* Christopher Whalen, *Washington & Wall Street: Does Barney Frank Have “Skin In The Game”?*, BREITBART (Sept. 6, 2013), <http://www.breitbart.com/Big-Government/2013/09/06/Washington-Wall-Street-Does-Barney-Frank-Have-Skin-in-the-Game>; *see also* Investor Protection and Securities Reform Act of 2010, 15 U.S.C. § 78o-11(e)(4)(C) (2012) (limiting the definition of QRM to be no broader than QM under § 129C of TILA).

154. Gao, *supra* note 1.

requiring securitizers of residential mortgages to keep some skin in the game.¹⁵⁵

A. *Legislative Purpose of QRM and QM Under the Dodd-Frank Act*

1. QRM Under The Securities Exchange Act of 1934 – Protecting Investors

A major concern of Congress while drafting the Dodd-Frank Act was how to draft legislation that would prevent a reoccurrence of Wall-Street-fueled bad lending and toxic securitization.¹⁵⁶ In 2009, the House of Representatives passed the Mortgage Reform and Anti-Predatory Lending Act (MRAPL) which introduced the credit risk retention rules.¹⁵⁷ MRAPL would have required creditors to retain some material portion of risk from MBS they sold to the secondary market.¹⁵⁸ The notion behind risk retention was that it was extremely important for creditors who participated in the secondary market to keep some “skin in the game.”¹⁵⁹ However, critics were concerned about how the credit risk retention legislation would work in practice, and whether the proposed exceptions to the rule were too narrow.¹⁶⁰

The MRAPL introduced the credit risk retention rule as an amendment to TILA § 129C.¹⁶¹ The amendment also provided an

155. See 156 CONG. REC. S3576 (daily ed. May 12, 2010) (statement of Sen. Johnny Isakson) (explaining the importance of only excluding mortgages with certain traits that would historically be good performing loans).

156. See *Mortgage Lending Reform: A Comprehensive Review of the American Mortgage System: Before the Subcomm. on Fin. Insts. and Consumer Credit*, 111th Cong. 173 (2009) (testimony of Julia Gordon, Center for Responsible Lending); 155 CONG. REC. H5316 (daily ed. May 7, 2009) (statement of Rep. Dennis Cardoza).

157. Mortgage Reform and Anti-Predatory Lending Act, H.R. 1728, 111th Cong. § 213 (2009) (this is the first time the credit risk retention legislation appears in any proposed bills).

158. *Id.* § 213(l)(1).

159. See generally H.R. REP. NO. 111-94, at 165 (2009) (discussing importance of having “skin in the game”); *Mortgage Lending Reform: A Comprehensive Review of the American Mortgage System: Hearing Before the Subcomm. on Fin. Insts. and Consumer Credit*, 111th Cong. 173 (2009) (testimony of Julia Gordon, Center for Responsible Lending) (same).

160. H.R. REP. NO. 111-94, at 165 (2009).

161. Mortgage Reform and Anti-Predatory Lending Act, H.R. 1728, 111th Cong. § 213

exception to the risk retention rule for creditors who sold mortgages that were QMs as defined under § 129C(c)(2)(A) to the secondary market.¹⁶² At this time, the QM definition used for the credit risk retention rule was the same QM definition used for the ability-to-repay rule under TILA.¹⁶³ It appeared that Congress's intent for credit risk retention was aligned with protecting consumers from receiving mortgages they could not afford by forcing creditors to use a higher underwriting standard if they did not want to retain risk from the mortgages they were originating.¹⁶⁴

However, the Dodd-Frank Act moved the credit risk retention rule from TILA to the Securities Exchange Act of 1934.¹⁶⁵ This removed the focus of risk retention from the mortgage originator to the securitizer.¹⁶⁶ The Dodd-Frank Act also created the CFPB, which is focused on protecting the consumer.¹⁶⁷ The creation of the CFPB allowed Congress's attention to focus on the concern that capital-market participants have little to no skin in the game.¹⁶⁸

Congress's goal was to make sure investors could have confidence in the quality of the assets that are utilized in securitization.¹⁶⁹ Congress believes that for securitizers to have "skin in the game" they need to retain a material amount of risk.¹⁷⁰ This aligns the interests of investors in asset-backed securities with the securitizers' economic interests.¹⁷¹ Therefore, securitizers who must retain risk "have a strong incentive to monitor the quality of the assets they purchase from originators, package into securities, and sell" on the

(2009).

162. *Id.* § 213(l)(1).

163. *See id.*

164. *See id.* Section 213 and 203 are both amendments to TILA and use the same definition for QM. *See id.*; *id.* § 203.

165. *See* Investor Protection and Securities Reform Act of 2010, 15 U.S.C. § 78o-11 (2012).

166. *See id.* (removing the credit risk retention rule from TILA and adding it as an amendment to the Securities Exchange Act of 1934).

167. *See* S. REP. NO. 111-176, at 11 (2010) (discussing why CFPB was created).

168. *See Consumer Protections in Financial Services: Past Problems, Future Solutions: Before the Comm. on Banking, Hous., and Urban Affairs*, 111th Cong. 17 (2009) (statement of Patricia A. McCoy, Professor of Law, University of Connecticut School of Law).

169. 156 CONG. REC. S3591 (daily ed. May 12, 2010) (statement of Sen. Mike Crapo) (speaking on the importance of risk retention to those who securitize assets).

170. S. REP. NO. 111-176, at 129 (2010).

171. *Id.*

secondary market.¹⁷² It was believed that no one party should be able to pass on all the risk to someone else.¹⁷³ Everyone should share the responsibility for the underlying financial products so that the securitizers of financial products “have as much skin in the game when they package the products as the consumers do when they buy them.”¹⁷⁴

When Congress shifted its focus to securitizers who retain credit risk, the exemption given to creditors who met QM standards under TILA was replaced with newly created QRM standards specific to investor safety.¹⁷⁵ The QRM definition was created to give an exemption to securitizers who sold RMBS containing only mortgages that had a very low risk of default even in a stressful economic environment, which combined high unemployment with sharp drops in home prices.¹⁷⁶ The drafters of the QRM standard believed that it would exempt only mortgages like those made in “the good-old-days.”¹⁷⁷ A good-old-day mortgage required that the consumer was actually qualified to borrow the loan amount, that there was a significant down payment from the borrower (or mortgage insurance in its place), and that the consumer had a good debt-to-income ratio.¹⁷⁸ Furthermore, the drafters of QRM believed that securitizing mortgages that have a 20% down payment and a high credit rating did not require the same level of skin in the game as mortgages that did not have those elements.¹⁷⁹

Although the drafters of QRM wanted to see a return to the type of mortgages originated in former times, there was heavy criticism of requiring a mandatory down payment for fear of creating standards that

172. *Id.*

173. *Enhancing Investor Protection and the Regulation of Securities Markets: Before the Comm. on Banking, Hous., and Urban Affairs*, 111th Cong. 3 (2009) (statement of Sen. Christopher J. Dodd, Chairman, Comm. on Banking, Hous., and Urban Affairs).

174. *Id.*

175. See 156 CONG. REC. S3575 (daily ed. May 12, 2010) (statement of Sen. Mary Landrieu) (moving, on behalf of the Senate Small Business Committee, to replace QM with QRM).

176. Edward Pinto, *A Qualified Residential Mortgage ≠ a Qualified Mortgage*, AM. ENTERPRISE INST. (Aug. 28, 2013, 3:00 PM), <http://www.aei-ideas.org/2013/08/a-qualified-residential-mortgage-%E2%89%A0-a-qualified-mortgage/>.

177. 156 CONG. REC. S3576 (daily ed. May 12, 2010) (statement of Sen. Johnny Isakson).

178. *See id.*

179. *Id.* (explaining the importance of only excluding risk retention for mortgages with certain traits that would historically be good performing loans).

would shut out qualified low- and moderate-income borrowers.¹⁸⁰ An initial amendment to the credit risk retention rule proposed a fixed 5% down payment requirement.¹⁸¹ The amendment was voted down in favor of another more flexible amendment with mortgage underwriting standards, a requirement to verify income and assets, and no minimum down payment requirement.¹⁸² Down payment requirements were still considered very important to the drafters of QRM, but it was thought that a QRM definition which required mortgage insurance could cover the risk for any down payment under 20% and allow access to credit for those individuals who could not afford to put 20% down.¹⁸³ The drafters of QRM hoped that regulators would ensure that a broad spectrum of qualified borrowers fell under the QRM exception umbrella.¹⁸⁴ Eventually, Congress adopted the Landrieu-Isakson amendment, with minor changes, which reflects the language defining QRM under of the Dodd-Frank Act.¹⁸⁵

In defining QRM, Section 941 of the Dodd-Frank Act states that any exception or exemption under the credit risk retention rule should meet the following criteria: (1) help ensure high quality underwriting standards for the securitizers and originators of assets that are securitized or available for securitization; and (2) encourage appropriate risk-management practices by the securitizers and originators of assets, improve the access of consumers and businesses to credit on reasonable terms, or otherwise be in the public interest and for the protection of investors.¹⁸⁶ Congress further guided the Agencies in creating the QRM definition by instructing them to look at underwriting and product features that historical loan performance data indicated results in a lower risk of default.¹⁸⁷

180. 156 CONG. REC. S3520 (daily ed. May 11, 2010) (statement of Sen. Christopher J. Dodd, Chairman, Comm. on Banking, Hous., and Urban Affairs) (stating that mandatory 5% down payment requirement in Corker amendment is overly burdensome).

181. *Id.* at S3519.

182. *See* 156 CONG. REC. S3574 (daily ed. May 12, 2010) (The Merkley Amendment passed by a 63-36 vote while the Corker Amendment lost by 42-57 vote.).

183. 156 CONG. REC. S10442 (Dec. 17, 2012) (statement of Sen. Johnny Isakson) (noting that need for a 20% down payment was not needed if lower down payments were coupled with mortgage insurance).

184. *Id.*

185. *See* H.R. REP. NO. 111-517, at 529 (2010) (Conf. Rep.).

186. Investor Protection and Securities Reform Act of 2010, 15 U.S.C. § 78o-11(e)(2) (2012).

187. *Id.* § 78o-11(e)(4).

These underwriting and product features include documentation and verification of the financial resources used to qualify a borrower.¹⁸⁸ Other features to be considered are the residual income of the borrower after all monthly obligations have been considered (debt-to-income ratio), the ratio of the housing payments of the borrower to the monthly income of the borrower (front-end ratio), and the ratio of total monthly installment payments of the borrower to the income of the borrower (back-end ratio).¹⁸⁹ Features such as mitigating the potential for payment shock on adjustable-rate mortgages, the presence or absence of mortgage insurance, and restricting the use of balloon payments, negative amortization, prepayment penalties, interest-only payments, and other high risk features should also be considered under the definition of QRM.¹⁹⁰ In addition to taking certain features into consideration for the QRM definition, the Dodd-Frank Act specifically prohibited the definition of QRM to be any broader than the definition of QM as provided under § 129C(c)(2) of TILA and regulations adopted thereunder by the CFPB.¹⁹¹

2. QM Under TILA – Protecting Consumers

Unlike the definition of QRM, QM was originally conceived before the financial crisis as part of proposed legislation aimed at preventing predatory lending.¹⁹² Congress was particularly concerned with lenders steering borrowers to mortgages that the consumer could not afford, did not provide a net tangible benefit to consumers, treated borrowers differently based on their race or their economic standing, or had other predatory characteristics.¹⁹³ In order to combat the problem of lenders steering borrowers into mortgages they could not afford, the ability-to-repay legislation was proposed.¹⁹⁴ Under the ability-to-repay

188. *Id.* § 78o-11(e)(4)(B)(i).

189. *Id.* § 78o-11(e)(4)(B)(ii)(I)-(III).

190. *Id.* § 78o-11(e)(4)(B)(iii)-(v).

191. *Id.* § 78o-11(e)(4)(C).

192. *See generally* Mortgage Reform and Anti-Predatory Lending Act of 2007, H.R. 3915, 110th Cong. § 203 (2007) (providing the first QM definition under TILA and a safe harbor and rebuttable presumption section).

193. 153 CONG. REC. H13965 (daily ed. Nov. 15, 2007) (statement of Rep. David Scott) (discussing the concerns that the proposed bill, with the QM definition, is supposed to remedy).

194. 12 C.F.R. § 1026.43(c) (2013) (ability to repay codified in CFPB regulations under

legislation, no creditor may make a residential mortgage loan unless the creditor makes a reasonable and good-faith determination based on verified and documented information that, at the time the loan is consummated, the consumer has a reasonable ability to repay the loan, according to its terms, all applicable taxes, insurance, and assessments.¹⁹⁵

Proposed legislation also included a safe harbor and rebuttable presumption to the ability-to-repay rule limiting liability on originators if the mortgages they sold met certain criteria.¹⁹⁶ Originally, proposed legislation provided an irrebuttable presumption for mortgages that met the definition of a QM and a rebuttable presumption for mortgages that met the definition of a “qualified safe harbor mortgage” (QSHM).¹⁹⁷ However, the QSHM definition was soon replaced with the QM definition.¹⁹⁸ The original definition of QM was narrow and included residential mortgages that constituted a first lien on a dwelling or real property that had an annual percentage rate¹⁹⁹ not equal to or in excess of certain securities issued by the Secretary of the Treasury.²⁰⁰ It also included any residential mortgage loan that was not a first lien on the dwelling or real property that had an annual percentage rate²⁰¹ not equal to or in excess of certain securities issued by the Secretary of the

TILA).

195. Mortgage Reform and Anti-Predatory Lending Act, 15 U.S.C. § 1639c(a)(1) (2012) (ability to repay under TILA).

196. *Id.* § 1639c(b).

197. H.R. 3915.

198. Mortgage Reform and Anti-Predatory Lending Act, H.R. 1728, 111th Cong. § 203 (2009) (showing that the definition of QSHM has been revised and replaced with QM).

199. First lien on a dwelling or real property that: “(I) has an annual percentage rate that does not equal or exceed the yield on securities issued by the Secretary of the Treasury under chapter 31 of title 31, United States Code, that bear comparable periods of maturity by more than 3 percentage points; or (II) has an annual percentage rate that does not equal or exceed the most recent conventional mortgage rate, or such other annual percentage rate as may be established by regulation under paragraph (6), by more than 175 basis points.” H.R. 3915 at § 203.

200. *Id.*

201. Not a first lien on the dwelling or real property that: “(I) has an annual percentage rate that does not equal or exceed the yield on securities issued by the Secretary of the Treasury under chapter 31 of title 31, United States Code, that bear comparable periods of maturity by more than 5 percentage points; or (II) has an annual percentage rate that does not equal or exceed the most recent conventional mortgage rate, or such other annual percentage rate as may be established by regulation under paragraph (6), by more than 375 basis points; and (iii) a loan made or guaranteed by the Secretary of Veterans Affairs.” *Id.*

Treasury.²⁰²

Many members of Congress worried that the narrow definition of QM was going to have the unintended consequence of restricting mortgage credit availability for traditional loans.²⁰³ Congress decided that the agency charged with defining QM should have the flexibility to expand the definition of QM to make the safe harbor as broad as possible while still preventing predatory lending.²⁰⁴ It did this by allowing the agency to prescribe regulations that “revise, add to, or subtract from the criteria that define a qualified mortgage upon a finding that such regulations are necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers.”²⁰⁵

Congress expanded the QM definition throughout the legislative process to include nontraditional mortgage products that met certain criteria and also offered alternative QM definitions.²⁰⁶ Congress left the final say over the definition of QM with the newly created CFPB by granting it the power to amend TILA, under which the QM definition falls.²⁰⁷ The CFPB created a broad QM definition in its final rule, providing a safe harbor and a rebuttable presumption that the borrower satisfies the ability-to-repay rules when a lender’s mortgages comply with the QM definition.²⁰⁸

B. *Congress Intended for QRM and QM to be Different*

One indication that Congress believed QRM should not mean QM is the simple fact that Congress chose different terms, showing that Congress thought that the different purpose behind each provision

202. *Id.*

203. See H.R. 1728, *The Mortgage Reform And Anti-Predatory Lending Act of 2009: Hearing Before the Comm. on Fin. Servs.*, 111th Cong. 4 (2009) (statement of Rep. Shelley M. Capito) (discussing her concerns with the narrow QM definition hurting credit availability and treating safe loans such as those insured by the FHA as predatory loans).

204. See H.R. REP. NO. 111-517, at 785 (2009).

205. *Id.*

206. See Mortgage Reform and Anti-Predatory Lending Act, 15 U.S.C. § 1639c (2013).

207. See generally Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), 12 U.S.C. § 5481(12)(O) (2010) (showing that TILA falls under the CFPB’s authority).

208. *Ability to Repay and Qualified Mortgage Standards Under the Truth in Lending Act (Regulation Z)*, CONSUMER FIN. PROTECTION BUREAU, <http://www.consumerfinance.gov/regulations/ability-to-repay-and-qualified-mortgage-standards-under-the-truth-in-lending-act-regulation-z/> (last visited Sept. 14, 2013).

justified a different definition.²⁰⁹ Furthermore, Congress moved the credit risk retention requirement from TILA²¹⁰ into the Securities Exchange Act of 1934.²¹¹ TILA was created with the intention of protecting consumers in their dealings with lenders and creditors.²¹² The Securities Exchange Act of 1934 was created to provide oversight of securities transactions in the secondary market, regulate the exchanges, and regulate broker-dealers in order to protect the investing public.²¹³ By moving the credit risk retention rule to the Securities Exchange Act of 1934, Congress was trying to protect investors purchasing ABS in the secondary market.²¹⁴

Originally under TILA, the credit risk retention rule used the QM definition for its exceptions.²¹⁵ However, Congress moved the credit risk retention rule into the Securities and Exchange Act of 1934 in order to protect investors in the secondary market by creating a completely new standard, QRM.²¹⁶ Furthermore, Congress sought to exempt risk retention for entities that packaged and sold MBS that met the requirements of a QRM,²¹⁷ which would have a very “low risk of default even in a stressful economic environment[] combining high unemployment with sharp drops in home prices.”²¹⁸ QRM meaning QM “clearly does not pass muster under any low risk standard” because QMs can have no down payment, a credit score in the bottom one-eighth of all scores, and a 50% or greater DTI ratio if approved by certain GSEs.²¹⁹

209. See 156 CONG. REC. S3575 (daily ed. May 12, 2010) (statement of Sen. Mary Landrieu) (showing the Senate Small Business Committee moved to define the QRM exception).

210. Mortgage Reform and Anti-Predatory Lending Act, H.R. 1728, 111th Cong. § 213 (2009) (showing that the original risk retention was set up under TILA).

211. Investor Protection and Securities Reform Act of 2010, 15 U.S.C. § 78o-11 (2013) (showing that the credit risk retention rule has been removed from TILA and added as an amendment to the Securities Exchange Act of 1934).

212. See generally Truth In Lending Act (TILA), 15 U.S.C. § 1601 (2013) (discussing the purpose of TILA).

213. See generally Securities Exchange Act Of 1934, 15 U.S.C. § 78b (2013) (discussing the purpose of the act).

214. See S. REP. NO. 111-176, at 129 (2010).

215. H.R. 1728.

216. See Investor Protection and Securities Reform Act of 2010, 15 U.S.C. § 78o-11 (2013).

217. See *id.*

218. Pinto, *supra* note 176 (original quotation omitted).

219. *Id.*

Another indication that QRM was not intended to mean QM is that Congress specifically created QRM when it could have easily preserved the QM definition. Indeed, QM was already in existence and was originally used as the standard for credit risk retention under TILA.²²⁰ If Congress intended for QRM to mean QM under the Securities Exchange Act of 1934, why not direct the CFPB to create the standard in TILA and tell the Agencies to adopt the CFPB's final definition? Congress did not do that because QM was meant to define a minimum loan standard while QRM was meant to define a low risk loan.²²¹ These two goals do not necessarily overlap.

Furthermore, the goals of borrowers and the goals of investors are completely different and should have protections that take those differences into account instead of trying to create a one-size-fits-all standard, which is a consequence of equating QRM and QM.²²² CFPB Director Richard Cordray even seemed surprised when the Agencies announced that QRM would mean QM when he stated that the "CFPB's ability-to-repay rule [defining QM] is consciously designed to protect consumers from unaffordable credit" and is "not a credit risk rule designed for investor protection which is what QRM is concerned with."²²³ Another high ranking official at the CFPB called the CFPB's "role in crafting both standards [QM and QRM] . . . a weird outcome."²²⁴ The shock stems from Congress's intention for QM to "boost underwriting standards while QRM exists to provide investors with a class of ultra-safe loans."²²⁵

Another signal that Congress did not intend for QRM to mean QM is the fact that QM was created with the intention of ensuring that the maximum number of traditional loans fell under the QM safe harbor umbrella.²²⁶ QM is also subject to change by CFPB regulation, which

220. See H.R. 1728 at § 213.

221. Pinto, *supra* note 176.

222. See Mike Ferullo, *Regulators Ease Standards for Mortgages Exempt From Risk Retention Mandate*, BANKING DAILY (Aug. 29, 2013), http://news.bna.com/bdln/BDLNWB/split_display.adp?fedfid=36037049&vname=bbdbulallissues&fcn=1&wsn=1&fn=36037049&split=0 (statement by Richard Cordray, Director of CFPB).

223. *Id.*

224. Joe Adler, *Why the CFPB Could Gain Monopoly Over Mortgage Rules*, AM. BANKER, Oct. 7, 2013, at 3.

225. See *id.*

226. Natter, *supra* note 8, at 12.

means that the QM definition can become broader at any time.²²⁷ If QM subsequently changes and becomes broader, then QRM will also become broader regardless of whether the additional mortgages included within QM are of very high credit quality.²²⁸ Regulators whose focus is primarily on a borrower's ability to repay likely will not be tailoring changes to the rule in order to address the capital markets goals of QRM.²²⁹ This approach does not coincide with Congress's intention to provide an exemption from keeping skin in the game for only those mortgages with a very high credit quality.²³⁰

Congress created the credit risk retention rule with the goal that securitizers would have some skin in the game.²³¹ Congress intended to give securitizers an exemption to risk retention if their financial products were made up of certain low risk mortgages that had features such as a high down payment or mortgage insurance, because the same level of risk retention would not be required due to the fact that these loans historically perform well.²³² With securitizers retaining credit risk, investors could have confidence in the quality of the assets that are utilized in a securitization.²³³

Defining QRM to mean QM greatly expands the universe of mortgages that may be securitized without the securitizer having to retain any risk.²³⁴ In 2012, 85% of residential mortgages were insured by the FHA or bought by Fannie Mae or Freddie Mac.²³⁵ Under the QRM-QM definition, 85% of residential mortgages could have been securitized and sold to investors without the securitizer keeping any

227. Mortgage Reform and Anti-Predatory Lending Act, 15 U.S.C. § 1639c(b)(3)(B)(i) (2013) (allowing QM to be revised, added to, or subtracted from).

228. See Credit Risk Retention, 78 Fed. Reg. 57,928, 57,991-92 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43) (commenting that if QRM=QM, any QM will now qualify for an exemption to risk retention under the new definition).

229. Adler, *supra* note 224.

230. Pinto, *supra* note 176 (discussing the purpose of QRM definition).

231. S. REP. NO. 111-176, at 129 (2010).

232. See 156 CONG. REC. S3576 (daily ed. May 12, 2010) (statement of Sen. Mary Landrieu) (explaining that certain features within loans would not require risk retention).

233. 156 CONG. REC. S3591 (daily ed. May 12, 2010) (statement of Sen. Mike Crapo).

234. See Credit Risk Retention, 78 Fed. Reg. 57,928, 57,979 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43).

235. Robert C. Pozen, *How to Create Another Housing Crisis*, WALL ST. J., Sept. 11, 2013,

<http://online.wsj.com/article/SB10001424127887324094704579065292392851168.html>.

skin in the game.²³⁶ Creating a broad QRM definition “could blunt the risk retention rule’s ability to raise market confidence” in mortgage securitizations which, of course, was its intended purpose.²³⁷ QRM meaning QM makes credit risk retention the exception while Congress intended credit risk retention to be the rule.²³⁸

Another sign that Congress did not intend for QRM to mean QM is that Congress specifically instructed the Agencies to look at underwriting and product features such as loans without prepayment penalties or balloon payments that historical loan performance data indicated resulted in a lower risk of default when defining QRM.²³⁹ By setting QRM to mean QM, Congress’s instructions are being disregarded because some mortgages may qualify as a QM even if the mortgages contain prepayment penalties or balloon payments.²⁴⁰ If QRM means QM, then the same high-risk features Congress did not want in QRMs could be exempt and securitized without the securitizer having to retain any risk.²⁴¹ Furthermore, a QM neither requires a down payment nor requires mortgage insurance in the absence of a down payment as Congress intended in order to qualify as a QRM.²⁴² This is a further indication that QRM was not meant to mean QM as defined under § 129C of TILA.

236. See Credit Risk Retention, 78 Fed. Reg. at 57,992 (showing GSE mortgages are QRM eligible).

237. Mark Zandi & Cristian deRitis, *The Skinny on Skin in the Game*, MOODY’S ANALYTICS (Mar. 11, 2011), <http://www.moodyanalytics.com/~media/Insight/Economic-Analysis/Housing/03-11-11-The-Skinny-on-Skin-in-the-Game.ashx> (discussing the risks of having a broad QRM definition).

238. See S. REP. NO. 111-176, at 129 (2010); *Enhancing Investor Protection and the Regulation of Securities Markets: Hearing Before the Comm. on Banking, Hous., and Urban Affairs*, 111th Cong. 3 (2009) (statement of Sen. Christopher J. Dodd, Chairman, Comm. on Banking, Hous., and Urban Affairs).

239. See Investor Protection and Securities Reform Act of 2010, 15 U.S.C. § 78o-11(e)(4) (2012).

240. See 12 C.F.R. § 1026.43(e)-(g) (section (e) gives the general definition for QM, (f) allows for certain loans to have balloon payments, and (g) allows for prepayment penalties for some loans).

241. See Credit Risk Retention, 78 Fed. Reg. at 57,991-92 (QRM is equal to QM).

242. 156 CONG. REC. S10442 (daily ed. Dec. 17, 2012) (statement of Sen. Johnny Isakson) (stating the need for mortgage insurance for individuals who could not meet a minimum down payment requirement under QRM).

C. *Negative Feedback Should Not Translate to QRM Meaning QM*

Although the Agencies received a large amount of negative feedback on the original QRM proposal, the Agencies need to look carefully at the complaining parties. Realtors were among the most vocal groups against a narrowly defined QRM standard.²⁴³ Realtors are incentivized to get consumers approved for any kind of loan, risky or not, so that they can sell homes and earn commissions.²⁴⁴ This is almost the exact opposite of Congress's goal of ensuring that QRMs are of very high credit quality.²⁴⁵ Investors, the group credit risk retention and QRM should protect, supported the kinds of loan-to-value, credit history, and debt-to-income factors the Agencies originally proposed.²⁴⁶ The Agencies should "be mindful of the points raised by commenters, [but] ultimately they must apply their experience and expertise" in the manner that Congress intended irrespective of the volume of negative comments.²⁴⁷

QRM might not have been intended to have a 20% down payment requirement, but its drafters relied on other protections such as mortgage insurance to keep QRMs of very high credit quality.²⁴⁸ Congress believed that by requiring mortgage insurance, it would ensure that the QRM exemption would "serve those consumers that could not afford a 20% down payment while putting substantial private capital at risk to drive underwriting discipline."²⁴⁹ The drafters of QRM wanted a broad spectrum of high-credit-quality mortgages to be exempt from credit risk retention because they would not require the same

243. See *Statement From NAR President Gary Thomas on Qualified Residential Mortgage Rule*, NAT'L ASS'N OF REALTORS (Aug. 28, 2013), <http://www.realtor.org/news-releases/2013/08/statement-from-nar-president-gary-thomas-on-qualified-residential-mortgage-rule>.

244. See Moshe Pollock, *How Do Real Estate Agents Get Paid?*, REALTOR.COM, <http://www.realtor.com/home-finance/homebuyer-information/how-do-real-estate-agents-get-paid.aspx?source=web> (last visited Oct. 4, 2013).

245. See Credit Risk Retention, 76 Fed. Reg. 24,090, 24,118 (proposed Apr. 29, 2011) (to be codified at 12 C.F.R. pt. 43).

246. Credit Risk Retention, 78 Fed. Reg. at 57,995.

247. See Margaret Chadbourn & Emily Stephenson, *U.S. proposes relaxed 'skin in the game' mortgage rules*, REUTERS (Aug. 28, 2013, 1:22 PM), <http://www.reuters.com/article/2013/08/28/us-usa-housing-regulations-idUSBRE97R05L20130828>.

248. See 156 CONG. REC. S10442 (daily ed. Dec. 17, 2012) (statement of Sen. Johnny Isakson) (stating that lower down payments can be countered with mortgage insurance).

249. *Id.*

amount of skin in the game.²⁵⁰ However, QRM meaning QM has sacrificed credit quality for exemption inclusivity. The re-proposed QRM definition does not provide for any down payment requirement or mortgage insurance which the drafters of QRM deemed extremely important.²⁵¹ The original QRM definition might be too narrow, but QRM meaning QM is too broad and goes against Congress's intended goal. The Agencies started at one extreme and have now reached the other, both of which are contradictory to Congress's intended goal.²⁵²

Despite Congress's intention, many would argue that QRM should mean QM.²⁵³ Many groups, including individuals, industry participants, insurance companies, public interest groups, state agencies, financial institutions, and trade organizations believe that "the original QRM definition was too narrow and would increase borrowing costs [and] reduce access to credit for borrowers who have higher levels of monthly debt or cannot come up with a 20% down payment."²⁵⁴ Not surprisingly, these are the same groups who made identical arguments against the final QM definition.²⁵⁵ Any set of fixed underwriting rules will exclude some creditworthy borrowers whether QRM is narrow, QRM means QM, or some medium is reached.²⁵⁶ Their argument is also belied by experience in Canada where most lenders insist on a down payment of at least 20% of the home's value, although the government provides some support to first-time and lower-income home buyers, and lenders look carefully at the borrower's ability to

250. *See id.*

251. *See id.*

252. *Compare* Credit Risk Retention, 78 Fed. Reg. 57,928, 57,991 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43) (showing the new requirements under QRM means QM, excluding down payments and not instating any mortgage insurance requirement), *with* Credit Risk Retention, 76 Fed. Reg. 24,090, 24,123 (proposed Apr. 29, 2011) (to be codified at 12 C.F.R. pt. 43) (demonstrating the original QRM definition included a 20% down payment requirement).

253. *See* Credit Risk Retention, 78 Fed. Reg. at 57,988-89 (stating that an overwhelming majority of commenters disliked the original proposed QRM definition).

254. Ferullo, *supra* note 222 (discussing QRM=QM and providing opinions of those who support QRM=QM).

255. *See* 155 CONG. REC. H5317 (daily ed. May 7, 2009) (statement of Rep. Pete Sessions) (relaying a message from the Mortgage Bankers Association (MBA) stating that "the bill's definition of 'qualified mortgage' is far too limited and will result in the unavailability of sound credit options to many borrowers and the denial of credit to far too many others").

256. Credit Risk Retention, 76 Fed. Reg. at 24,118.

make monthly payments.²⁵⁷ Despite the higher credit standards, the homeownership rate is higher in Canada than in the United States.²⁵⁸ Regardless of any down payment requirement, the Agencies' QRM definition should adopt a provision requiring mortgage insurance for those individuals who cannot make reasonable down payments in order to comply with Congress's intentions.²⁵⁹

Critics also claimed that the narrow QRM standard "would become a new government-approved standard and lenders would be reluctant to originate mortgages that did not meet that standard."²⁶⁰ However, the Agencies' original QRM standard was meant to combat those fears by excluding only a small number of loans, leaving a larger non-QRM mortgage market requiring risk retention.²⁶¹ All else being equal, a larger market of non-QRMs would allow ABS backed by non-QRM residential mortgages to be routinely issued and purchased by a wide variety of investors, resulting in the market for such securities being relatively liquid.²⁶² The Agencies believed "the broader the definition of a QRM, the less liquid the market ordinarily would be for residential mortgages falling outside the QRM definition."²⁶³ QRM meaning QM would over-broaden the market and create the exact problem critics have identified while allowing securitizers to avoid having skin in the game.²⁶⁴ The drafters of QRM under the Dodd-Frank Act intended for QRMs to be the "new gold standard" for residential mortgages, allowing for a broad and liquid non-QRM market.²⁶⁵

Critics believe that a narrow QRM definition could cause a reduction in credit availability, while most experts believe when QM goes into effect there will be some retrenchment in credit availability.²⁶⁶

257. Pozen, *supra* note 235.

258. *Id.*

259. See 156 CONG. REC. S10442 (daily ed. Dec. 17, 2012) (statement of Sen. Johnny Isakson).

260. Credit Risk Retention, 78 Fed. Reg. 57,928, 57,933 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43).

261. Credit Risk Retention, 76 Fed. Reg. at 24,118.

262. *Id.*

263. *Id.*

264. See generally Pozen, *supra* note 235 (claiming that QRM meaning QM is a good way to cause another mortgage crisis).

265. 156 CONG. REC. S10441 (daily ed. Dec. 17, 2012) (statement of Sen. Johnny Isakson).

266. Rachel Witkowski, 'Safe Harbor' for QM Loans May Not Protect Banks, AM. BANKER, Sept. 5, 2013, http://www.americanbanker.com/issues/178_172/safe-harbor-for-

Initially, either definition will likely lead to some restriction of credit. Congress intended QRMs to be mortgages that have a very low risk of default in stressful economic environments that combine high unemployment with sharp drops in home prices.²⁶⁷ Academic research and the Agencies' own analyses indicate that taking into consideration credit history and LTV ratios (down payments) or the use of mortgage insurance to cover low down payments are significant factors in determining the probability of mortgage default.²⁶⁸ These factors are what Congress intended to be included in a QRM even if some borrowers may be adversely affected.²⁶⁹ Congress intended to prevent a repeat of the financial crisis, and that means that securitizers must have some skin in the game.²⁷⁰ Therefore, QRM should not mean QM and the Agencies should adopt a narrower definition of QRM.

VI. CONCLUSION

After the 2008 financial crisis, Congress set out to adopt legislation that would provide borrowers with mortgages they could reasonably afford and protect investors from being sold toxic MBS.²⁷¹ Congress created the CFPB and the ability-to-repay rule (defining QM) to protect consumers from unaffordable credit.²⁷² Congress instructed the Agencies to define QRM as a credit risk retention rule to meet Congress's stated goal of protecting investors.²⁷³ When Congress instructed the Agencies to define QRM, it did not intend for QRM to mean QM or for QRM to have a 30% down payment requirement,

qm-loans-may-not-protect-banks-1061822-1.html.

267. Pinto, *supra* note 176.

268. See Credit Risk Retention, 78 Fed. Reg. 57,928, 57,990 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43).

269. 156 CONG. REC. S3590-91 (daily ed. May 12, 2010) (statement of Sen. Mike Crapo).

270. See *Mortgage Lending Reform: A Comprehensive Review of the American Mortgage System: Hearing Before the Subcomm. on Fin. Insts. and Consumer Credit*, 111th Cong. 173 (2009) (testimony of Julia Gordon, Center for Responsible Lending); *Enhancing Investor Protection and the Regulation of Securities Markets: Hearing Before the Comm. on Banking, Hous., and Urban Affairs*, 111th Cong. 3 (2009) (statement of Sen. Christopher J. Dodd, Chairman, Comm. on Banking, Hous., and Urban Affairs).

271. See generally Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), Pub. L. No. 111-203, 124 Stat. 1376 (2010) (creating the ability-to-repay and credit risk retention rules).

272. Ferullo, *supra* note 222.

273. *Id.*

which the Agencies mandated in their alternative QRM definition, QM-plus.²⁷⁴

Rather, Congress was trying to protect two distinct groups—borrowers and investors—whose interests do not always overlap. The credit risk retention rule was moved out of TILA and into the Securities Exchange Act of 1934, showing Congress's intent to protect investors.²⁷⁵ Congress created QRM to ensure securitizers had skin in the game when they sold MBS to the investing public.²⁷⁶ Defining QRM to mean QM allows securitizers to package mortgages that are not very low risk without having to retain any of the credit risk.²⁷⁷ If Congress intended for QRM to mean QM, it could have easily stipulated that the Agencies define QRM according to the CFPB's final QM definition or kept QM for both TILA and the Securities Exchange Act of 1934. Congress did not so intend, however, because it wanted risk retention to be the rule and not the exception.²⁷⁸ Consequently, QRM should not mean QM and the Agencies should adopt a narrower definition of QRM.

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274. See Credit Risk Retention, 78 Fed. Reg. 57,928, 57,994 (proposed Sept. 20, 2013) (to be codified at 12 C.F.R. pt. 43).

275. See Mortgage Reform and Anti-Predatory Lending Act, H.R. 1728, 111th Cong. § 213 (2009) (original risk retention set up under TILA); Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), § 941 Pub. L. No. 111-203, 124 Stat. 1376 (2010) (risk retention now under the Securities Exchange Act of 1934).

276. S. REP. NO. 111-176, at 129 (2010).

277. See generally Pinto, *supra* note 176 (discussing why QRM should not mean QM).

278. Credit Risk Retention, 78 Fed. Reg. at 57,995.

APPENDIX

Key Differences Between Original QRM Proposal And Final QM Definition		
Eligibility Criteria	Original QRM Proposal	QM
Eligible Loans	<ul style="list-style-type: none"> • First-lien mortgages only • Requires at least one unit to be the principal dwelling of the borrower 	<ul style="list-style-type: none"> • Allows first liens and subordinate liens to qualify • Includes any closed-end loan secured by any dwelling (e.g., home purchase, refinances, home equity lines, and second or vacation homes)
Borrower Credit History	<ul style="list-style-type: none"> • Sets derogatory factors that must not be met by the borrower 	
Loan-to-Value Ratio (LTV)	<ul style="list-style-type: none"> • 80% or less for purchase mortgage transactions • 75% or less for rate and term refinancing • 70% or less for cash-out refinancing 	
Down Payment Requirement	<ul style="list-style-type: none"> • 20% on the purchase of any one-to-four family property 	
Qualifying Appraisal	<ul style="list-style-type: none"> • Supported by a written appraisal that conforms to generally accepted 	

	appraisal standards, as evidenced by the Uniform Standards of Professional Appraisal Practice, the appraisal requirements of the Federal banking agencies, and applicable laws.	
Ability to Repay	<ul style="list-style-type: none"> • Front-end debt-to-income ratio cannot exceed 28% • Back-end debt-to-income ratio cannot exceed 36% 	<ul style="list-style-type: none"> • Debt-to-income ratio cannot exceed 43% (does not break out debt-to-income ratios into front or back end)
Assumability	<ul style="list-style-type: none"> • Not assumable by any person who was not a borrower under the original mortgage transaction 	
Government Sponsored Enterprises (GSE) Inclusion		<ul style="list-style-type: none"> • QM if eligible for purchase, guarantee or insurance by a GSE, HUD, the Veterans Administration, U.S. Department of Agriculture, or Rural Housing Service