

QM: CURRENT VIEW ON ESSENT MI PREMIUMS

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The Dodd-Frank Act requires lenders to determine whether borrowers have the ability to repay their mortgages, but creditors can assume that borrowers have met the ability-to-repay requirement (ATR) if their loans are deemed Qualified Mortgages (QM). The Consumer Financial Protection Bureau's (CFPB) final QM rule became effective on January 10, 2014.

Standard QM Requirements. A loan generally cannot be a QM if it has any of the following features:

- negative amortization
- interest-only payments
- balloon payments
- a term greater than 30 years
- points and fees that are greater than 3% of the total loan amount (with higher caps applying to small loans).

The standard QM rule also requires the borrower to have a debt-to-income (DTI) ratio of 43% or less, as measured under strict regulatory standards, unless the temporary QM category applies (see next column).

Temporary QM Category. The final rule provides for a second, temporary QM category that allows for more flexible underwriting requirements. To qualify under the temporary QM definition, a mortgage must meet the general product feature and points-and-fees requirements, and be eligible to be purchased or guaranteed by the GSEs (while in conservatorship or until 2021, whichever is earlier), the Department of Agriculture or Rural Housing Service. The FHA and VA have published their own, permanent QM standards for loans they insure or guarantee.

In May 2013, the FHFA directed the GSEs to limit purchases after January 10, 2014 to those that meet the QM criteria (i.e., generally those loans that are fully amortizing, have terms of 30 years or less and have points and fees representing 3% or less of the total loan amount).

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QM Safe Harbors. The final rule provides a “safe harbor” for standard QM loans with Annual Percentage Rates (APRs) below the “higher-priced” threshold of 150 basis points over the Average Prime Offer Rate (APOR), and a “rebuttable presumption” for standard QM loans with an APR at or above that threshold. This means that a mortgage can be:

- a safe harbor QM because its APR is below the 150 basis points threshold and it either (i) meets the standard QM definition (limited to loans with DTIs of 43% or less) or (ii) is GSE-eligible
- a higher-priced QM with rebuttable presumption of compliance, but not a safe harbor
- a mortgage loan that must meet the ATR requirement unassisted by any presumptions (see next column).

ATR Determinations. Under the final rule, lenders making QM or non-QM loans must generally consider most or all of the following factors:

- income or assets
- employment status
- credit history
- monthly payment of principal and interest on mortgage
- monthly payment for mortgage-related obligations (e.g., property taxes)
- monthly payment on any simultaneous loan associated with the property
- other debt obligations
- monthly DTI ratio (or residual income) with the mortgage



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Points and Fees Test:

If the points and fees for a loan are in excess of 3% of the total loan amount (with higher caps applying to small loans), the loan cannot qualify for the

safe harbor or have the protection of a rebuttable presumption. The treatment of MI premiums as a component of the points and fees calculation can be a key

determinant of whether a loan can be in the safe harbor (or receive a presumption) or is ineligible for such protection.

Our current view of Essent MI premium treatment is as follows:

ESSENT MI PRODUCT	INCLUDED IN POINTS & FEES CALCULATION?	NOTES
BPMI Deferred or Standard Monthly (Refundable and Non-Refundable)	No	Periodic payments including any portion of an initial periodic payment due at closing are not included in the points and fees calculation.
BPMI Annual (Refundable and Non-Refundable)	No	Same as above.
BPMI Non-Refundable Singles or Split Premiums	Yes	Non-refundable single or upfront premium is included in the points and fees calculation.
BPMI Refundable Singles or Split Premiums	Yes, it is prudent to include the entire upfront premium until the law is clarified.	By rule, in order to exclude, the premium paid by the borrower at closing up to the FHA rate (currently 175 bps) must be refundable on a pro rata basis and the refund must be automatic upon loan payoff. Amounts in excess of the FHA rate are always included. (See also Disclosure below.)
LPMI Monthly or Singles (Non-Refundable)	No	If MI premium is reflected in the interest rate, it is not included in the points and fees calculation.

Sellers Points:

Payments by a seller toward finance charges — so-called “seller’s points” — are not included as finance charges in the points and

fees calculation as long as the consumer is not legally bound to the creditor for the charges. MI premiums are finance charges,

therefore, a seller’s payment of an upfront MI premium would not count toward the points and fees test.

Note: A loan that is not a QM can still be appropriate as long as a reasonable, good-faith determination has been made that the borrower is able to repay. You can continue to use the same underwriting guidelines you have used in the past to make loans that have generally performed well, as long as you document the information you considered. You can learn more about the ATR requirement at consumerfinance.gov/Regulations.

Disclosure: The above material has been prepared for general information purposes only. It is not intended as and should not be relied upon as legal advice. There is uncertainty with regard to the upfront portion of the Refundable BPMI

Single, as the QM rule does not define “pro rata.” The CFPB staff has informally noted that the interpretation of “pro rata” is governed by any applicable definition in state law or contract, and in the absence of such, they offered a perspective that a pro rata refund is one that is proportionate to the remaining policy life. While Essent’s five-year cancellation schedule has been approved by state insurance regulators as generally providing pro rata refunds, there remains uncertainty, which may ultimately be resolved in the various courts in which loan-level litigation may be pursued, or by more formal regulatory guidance from the CFPB.

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