

## INFOBYTES SPECIAL ALERT: VA ADOPTS ITS QM RULE

MAY 16, 2014

On May 9, 2014, the Department of Veterans Affairs (the “VA”) issued an [interim final rule](#) defining what constitutes a “qualified mortgage” (“QM”) for purposes of the loans it guarantees, insures, or originates.<sup>1</sup> The VA stated that, to quell persistent uncertainty among lenders regarding the treatment of VA loans under the temporary QM definition established by the Consumer Financial Protection Bureau (“CFPB”), it was adopting a rule designating all VA loans as QMs and all VA loans other than a subset of VA streamlined refinancings as safe harbor QMs.

The following chart illustrates the QM status of VA loans:

<b>VA Guaranteed or Insured Loans</b> (except streamlined refinancings)	<b>VA Guaranteed or Insured Streamlined Refinancings</b> (Interest Rate Reduction Refinancing Loans or “IRRRLs”)	<b>VA Originated Loans</b> <ul style="list-style-type: none"> <li>• VA Direct</li> <li>• Native American Direct</li> <li>• Vendee</li> </ul>
Safe Harbor QMs <sup>2</sup>	Safe Harbor QMs if: <ol style="list-style-type: none"> <li>(1) Loan being refinanced was originated at least 6 months before closing date of refinancing;</li> <li>(2) Veteran was not more than 30 days past due during the 6-month period;</li> <li>(3) The recoupment period for financed fees and charges does not exceed 36 months; and</li> <li>(4) Income is verified (unless the loan is exempt from such requirements)<sup>3</sup></li> </ol> IRRRLs that are not Safe Harbor QMs are Rebuttable Presumption QMs <sup>4</sup>	Safe Harbor QMs <sup>5</sup>

<sup>1</sup> Department of Veterans Affairs, Loan Guaranty: Ability-to-Repay Standards and Qualified Mortgage Definition under the Truth in Lending Act, 79 Fed. Reg. 26620 (May 9, 2014) [hereinafter “Interim Final Rule Release”].

<sup>2</sup> 38 C.F.R. § 36.4300(b).

<sup>3</sup> 38 C.F.R. § 36.4300(c)(1).

<sup>4</sup> 38 C.F.R. § 36.4300(c)(2).

<sup>5</sup> 38 C.F.R. § 36.4500(c). The VA defined “vendee loan” as “a loan made by the Secretary for the purposes of financing the purchase of property acquired pursuant to [38 U.S.C. chapter 37]” as a result of foreclosures in the guaranteed loan program. 38 C.F.R. § 36.4501; see also Interim Final Rule Release, 79 Fed. Reg. at 26623.

## EFFECTIVE DATE

The VA's rule took immediate effect upon publication on May 9, 2014, but the VA will accept comments on potential amendments and clarifications until June 9, 2014. The VA stated that it would exercise all reasonable efforts to publish a final rule addressing the comments in early August in order to provide lenders with certainty.<sup>6</sup>

## INCOME VERIFICATION FOR STREAMLINED REFINANCINGS (IRRRLS)

The VA explained that the purpose of its IRRRL streamlined refinancing program “is to place veterans into a better financial position by (i) reducing their interest rate in effect lowering their payment, (ii) reducing the term of the loan which would reduce the total of payments on the loan, or (iii) reducing their concern for market fluctuations by converting a loan from an ARM to a fixed rate.”<sup>7</sup> IRRRLs can only be used to refinance VA guaranteed loans and to pay for closing costs. IRRRLs cannot be used as “cash out” refinancings.<sup>8</sup>

Noting that the CFPB declined to exempt IRRRLs from the ability-to-repay requirement under its rule due to consumer advocate concerns about serial refinancing and equity stripping, the VA subjected refinancings of loans that had not been “seasoned” for at least 6 months to the rebuttable presumption instead of the safe harbor.<sup>9</sup> In addition, the VA established the following requirements for IRRRLs that are exempt from income verification requirements:

- i. The veteran is not 30 days or more past due on the existing loan;
- ii. The IRRRL would not increase the principal balance outstanding on the existing loan, except to the extent of fees and charges allowed by VA;
- iii. Total points and fees payable in connection with the IRRRL will not exceed 3% of the new loan amount (in addition to meeting VA limitations on fees and charges);
- iv. The interest rate on the IRRRL will be lower than the interest rate on the existing loan, unless the borrower is refinancing from an adjustable rate to a fixed-rate loan under VA guidelines;
- v. The IRRRL will be subject to a payment schedule that will fully amortize the loan consistent with VA regulations;
- vi. The terms of the IRRRL will not result in a balloon payment; and
- vii. Both the existing loan and the IRRRL satisfy all other VA requirements.<sup>10</sup>

## INDEMNIFICATION DEMANDS

Like the CFPB and the Department of Housing and Urban Development (“HUD”) for loans insured by the Federal Housing Administration (“FHA”), the VA stated that an indemnification demand or resolution of a

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<sup>6</sup> *Interim Final Rule Release*, 79 Fed. Reg. at 22620-21.

<sup>7</sup> *Id.* at 26624.

<sup>8</sup> *Id.* at 26625.

<sup>9</sup> *Id.* at 26625.

<sup>10</sup> 38 C.F.R. § 36.4340(b)(2).

demand “may result from facts that could allow a change to qualified mortgage status, but the existence of an indemnification does not per se remove qualified mortgage status.”<sup>11</sup>

## OTHER DIFFERENCES FROM CFPB TEMPORARY QM DEFINITION

Emphasizing its mission of serving veterans and its strong underwriting requirements and fee and term limitations, the VA stated that, “[t]o the extent there are differences between CFPB’s definition and VA’s, VA intends for its definition of qualified mortgage to loans guaranteed, insured, or made by VA to preempt rules that may seem contrary to VA’s.” The VA specifically noted that “[t]his would include those loans which would fit under VA’s definition, but not necessarily under the CFPB definition (i.e., negative amortization, documentation requirements for IRRRLs, minimum FICO score documentation, and . . . debt-to-income ratios).”<sup>12</sup>

Significantly, except as noted above for certain IRRRLs, it appears that VA loans are not subject to the requirements in the CFPB’s rule generally limiting points and fees on QMs to 3% of the loan amount. However, the VA imposes its own fee limitations.<sup>13</sup>

## WHAT’S LEFT?

The VA’s rule follows the adoption of a QM rule for FHA loans by HUD in December 2013.<sup>14</sup> The only agency that has not thus far used its authority to adopt its own QM definition is the Department of Agriculture. As a result, the CFPB’s temporary QM definition will continue to apply to loans guaranteed by the Department of Agriculture or insured by the Rural Housing Service.<sup>15</sup> Similarly, the CFPB’s temporary QM definition will continue to apply to loans that are eligible to be purchased or guaranteed by Fannie Mae, Freddie Mac, or any successor entity for as long as those entities remain under the conservatorship or receivership of the Federal Housing Finance Authority or until January 10, 2021, whichever is earlier.<sup>16</sup>

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<sup>11</sup> 38 C.F.R. § 36.4300(d).

<sup>12</sup> *Id.* at 26623.

<sup>13</sup> 38 C.F.R. § 36.4313.

<sup>14</sup> Department of Housing and Urban Development, *Qualified Mortgage Definition for HUD Insured and Guaranteed Single Family Mortgages*, 78 Fed. Reg. 75215 (Dec. 11, 2013)

<sup>15</sup> 12 C.F.R. § 1026.43(e)(4)(ii)(D)-(E) and (iii)(A).

<sup>16</sup> 12 C.F.R. § 1026.43(e)(4)(ii)(A) and (iii)(B); Cmts. 43(e)(4)-2 and -3.