Comments of

Consumer Federation of America, National Consumer Law Center (on behalf of its low-income clients), Consumer Action, Americans for Financial Reform, the Public Justice Center, the National Association of Consumer Advocates, Prosperity Now (formerly CFED), the Empire Justice Center, Atlanta Legal Aid Society, Inc., and the National Fair Housing Alliance

to the

Consumer Financial Protection Bureau

Regarding the Notice of Assessment

of Ability-to-Repay/Qualified Mortgage Rule and Request for

Public Comment

(Docket No. CFPB-2017-0014)

82 Fed. Reg. 25246

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I. Introduction

Thank you for the opportunity to comment on the Consumer Financial Protection Bureau's Request for Information Regarding the ability-to-repay/Qualified Mortgage (ATR/QM) Rule. The Consumer Federation of America,[1] the National Consumer Law Center,[2] on behalf of its low-income clients, Consumer Action,[3] Americans for Financial Reform,[4] the Public Justice Center,[5] the National Association of

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[1] **Consumer Federation of America** (CFA) is a nonprofit association of some 300 national, state, and local pro-consumer organizations created in 1968 to represent the consumer interest through research, advocacy, and education

[2] The **National Consumer Law Center, Inc.** (NCLC) is a non-profit Massachusetts corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of practice treatises on consumer credit laws and unfair and deceptive practices. NCLC attorneys regularly testify in Congress and provide comprehensive comments to the federal agencies on consumer regulations.

[3] **Consumer Action** has been a champion of underrepresented consumers since 1971. A national, nonprofit 501(c)(3) organization, Consumer Action focuses on financial education that empowers low to moderate income and limited-English-speaking consumers to financially prosper. It also advocates for consumers in the media and before lawmakers and regulators to advance consumer rights and promote industry-wide change particularly in the fields of credit, banking, housing, privacy, insurance and utilities. www.consumer-action.org

[4] **Americans for Financial Reform** (AFR) is a coalition of more than 200 consumer, investor, labor, civil rights, business, faith-based, and community groups that works through policy analysis, education, advocacy, and outreach to lay the foundation for a strong, stable, and ethical financial system. AFR was formed to advocate for the passage of the legislation that became Dodd-Frank and continues to protect and advance the reforms in that legislation, including by advocating for the full implementation of the housing policy reforms. A list of AFR member organizations is available at http://ourfinancialsecurity.org/about/our-coalition/

[5] The **Public Justice Center** works with people and communities to confront the laws, practices, and institutions that cause injustice, poverty, and

Consumer Advocates,[6] Prosperity Now (formerly CFED),[7] the Empire Justice Center,[8] Atlanta Legal Aid Society, Inc.,[9] and the National Fair Housing Alliance[10] submit these comments. [11]

discrimination. We advocate in the courts, legislatures, and government agencies, educate the public, and build coalitions, all to advance our mission of "pursuing systemic change to build a just society."

[6] The **National Association of Consumer Advocates (NACA)** is a nonprofit association of more than 1,500 consumer advocates and attorney members who represent hundreds of thousands of consumers victimized by fraudulent, abusive and predatory business practices. As an organization fully committed to promoting justice for consumers, NACA's members and their clients are actively engaged in promoting a fair and open marketplace that forcefully protects the rights of consumers, particularly those of modest means.

[7] **Prosperity Now** (formerly CFED) empowers low- and moderate-income households to build and preserve assets by advancing policies and programs that help them achieve the American Dream, including buying a home, pursuing higher education, starting a business and saving for the future. As a leading source for data about household financial security and policy solutions, Prosperity Now understands what families need to succeed. We promote programs on the ground and invest in social enterprises that create pathways to financial security and opportunity for millions of people.

[8] The **Empire Justice Center** is a statewide, multi-issue, multi-strategy public interest law firm focused on changing the "systems" within which poor and low income families live. With a focus on poverty law, Empire Justice undertakes research and training, acts as an informational clearinghouse, and provides litigation backup to local legal services programs and community based organizations. As an advocacy organization, we engage in legislative and administrative advocacy on behalf of those impacted by poverty and discrimination. As a non-profit law firm, we provide legal assistance to those in need and undertake impact litigation in order to protect and defend the rights of disenfranchised New Yorkers.

[9] **Atlanta Legal Aid Society, Inc.** is a nonprofit organization founded in 1924 that provides civil legal assistance to individuals and families of limited financial means in the Atlanta metropolitan area. Priority cases include housing, consumer fraud, employment, education, health, spouse abuse and child custody cases. For more than 29 years, Atlanta Legal Aid Society has represented homeowners who are facing the loss of their homes, have been targeted for predatory mortgage lending or servicing practices, and/or have been wrongfully denied loan modifications or other foreclosure prevention alternatives. Most of these clients are longtime homeowners, elderly and/or

The ability-to-repay rule has made a significant, positive impact in the lives of homeowners and has contributed to the restoration of a functioning mortgage market. This was crucial after the Great Recession rolled back a generation of progress on asset and wealth building through homeownership while decimating the economy. While further improvements to the rule are needed, the rule has restored common-sense principles to the origination market and has done so without restricting access to credit.

In these comments, we offer a number of recommendations to strengthen the rule. We discuss five of these in detail in sections III through VI of these comments. The other recommendations are briefly discussed in the last section of these comments, along with views regarding the assessment itself. The five recommendations discussed in detail are:

- Clarify that land installment contracts are subject to the TILA ability-to-repay rule;
- Exclude land installment contracts from Qualified Mortgage eligibility;
- Re-evaluate Appendix Q to promote its effectiveness;
- Keep the QM patch; and
- Subject high-cost open-end credit to the same stringent ability-to-repay analysis as high-cost closed-end credit.

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disabled living on modest retirement or disability income, or families experiencing layoffs or substantially reduced wages.

[10] **National Fair Housing Alliance** (NFHA). Founded in 1988, the National Fair Housing Alliance is a consortium of more than 220 private, non-profit fair housing organizations, state and local civil rights groups, and individuals from 37 states and the District of Columbia. Headquartered in Washington, DC, NFHA, through comprehensive education, advocacy and enforcement programs, provides equal access to housing for millions of people.

[11] These comments were written by Alys Cohen, Sarah Bolling Mancini, and Andrew Pizor of NCLC and Barry Zigas of CFA.

II. The ability-to-repay rule: safer lending without restricting access to credit

a. The ability-to-repay rule has made loans safer for consumers.

The ATR/QM provisions of the Dodd-Frank Act were enacted in response to the widespread pre-crisis sale of mortgages having unsustainable features by lenders using shoddy or even fraudulent underwriting practices. The rule was meant to align creditors' and borrowers' interests by creating an enforceable obligation for creditors to determine a borrower's ability to repay a loan and to document and verify key items like income and assets. We believe it has done this successfully.

Since the financial crisis, loans with abusive terms and conditions, such as "exploding" ARMs, balloon notes, no-doc and low-doc underwriting, and interest-only loans, have virtually disappeared—a positive outcome for everyone. The ATR/QM rule ensures that they will not return.

b. The ability-to-repay rule has not reduced access to credit.

Despite claims to the contrary, credit is currently tight because of market forces and lender over-correction—not because of the ability-to-repay rule. According to the Urban Institute, the ability-to-repay rule has only had a "small" impact on mortgage availability.[12] Instead, there is ample proof that other factors are causing the present limits on access to credit.

The share of adjustable rate mortgages is one sign that market forces are having a larger impact than the ATR rule. The share of ARMs has varied across sectors—GSE and portfolios—but has not shown a significant decline since the rule's adoption. For example, as

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[12] Bing Bai, et al., *Has the QM Rule Made it Harder to Get a Mortgage?,* Urban Institute (Mar. 2016) *available at* http://www.urban.org/sites/default/files/publication/78266/2000640-Has-the-QM-Rule-Made-It-Harder-to-Get-a-Mortgage.pdf.

Urban explained, the share of ARMs in the Primary Mortgage Market Survey declined from 4.5 percent to slightly under 4 percent in the years since the rule took effect.[13] But ARMs as a share of portfolio lending peaked *after* the rule's adoption at slightly more than 25 percent.. And the ARM share for GSEs was unaffected, remaining about the same before and after adoption. "In short," the Institute concluded, "QM does not seem to have had an effect on the ARM share, which is governed principally by the absolute level of interest rates, with the shape of the curve a contributing factor."[14] Creditors had stopped offering ARMs with unsustainable features well before the rule in response to their high failure rates. The rule's adoption merely codified these practices and the evidence suggests that the market has adapted without unreasonably reducing ARM availability when appropriate.

Another example comes from the OCC's Survey of Credit Underwriting Practices. Aspects of the Dodd-Frank Act began to take effect in 2011. The ATR rule took effect in January 2014. Yet, in December 2016, the OCC announced "[u]nderwriting practices among national banks and federal savings associations . . . eased for a fourth consecutive year . . . ."[15] This means that throughout the rollout of the Dodd-Frank Act and the ATR rule, lenders have continued to ease their credit standards. If the ATR rule was making credit tight, the OCC should have found lenders to be tightening standards in 2014. Instead, standards have gradually relaxed the further we get from the peak of the crisis.

[13] *"After hitting peak levels in summer 2014, interest rates began to decline, and the ARM share for all three channels followed. Notwithstanding the QM rule, the ARM share in 2014 was generally higher than in 2013. It has declined slightly in 2015 in response to the drop in interest rates starting in September 2014." Id.*

[14] *Id.*

[15] Office of the Comptroller of the Currency, press release, Underwriting Standards Ease for Fourth Consecutive Year, OCC Survey Shows (2016), available at https://www.occ.treas.gov/news-issuances/news-releases/2016/nr-occ-2016-159.html.

According to the OCC, "[t]he easing standards reflect the banks' response to competitive pressures, expanding credit risk appetites, and a desire for loan growth."[16] The OCC's Chief National Bank Examiner noted that "this movement is consistent with past credit cycles at a similar stage . . . ."[17] Access to credit is currently limited because creditors voluntarily adopted tighter credit underwriting standards in response to the foreclosure crisis. But their standards are relaxing over time, as indicated by the OCC's survey.

Other factors, including additional fees in the form of loan level price adjustments (LLPAs) at Fannie and Freddie, coupled with higher private mortgage insurance premiums for loans most likely to serve low-wealth borrowers, have raised the price of credit significantly. Similarly, lender responses to FHA-related enforcement actions have resulted in fewer FHA loans being made to borrowers not well served by the GSEs.

As a result of these factors, overall origination volumes have declined since 2010, and the Urban Institute has estimated that as many as 5 million consumers who would have received loans under normal credit standards in the 2001-2004 period have been shut out of the system since under the 2009-2014 period.[18] While their most recent Housing Credit Availability Index shows some expansion of credit, Urban notes that "Significant space remains to safely expand the credit box. If the current default risk was doubled across all channels, risk would still be well within the precrisis standard of 12.5 percent from 2001 to 2003 for the whole mortgage market."[19]

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[16] *Id.*

[17] *Id*.

[18] Bing Bai, et al., *Tight Credit Standards Prevented 5.2 Million Mortgages Between 2009-2014*, Urban Institute Housing Wire, (Jan. 28, 2016), *available at* http://www.urban.org/urban-wire/tight-credit-standards-prevented-52-million-mortgages-between-2009-and-2014.

[19] *Housing Credit Availability Index,Q12017,* Urban Institute, July 12, 2017 http://www.urban.org/policy-centers/housing-finance-policy-center/projects/housing-credit-availability-index

We agree that access to credit is currently more difficult for low- and moderate-income consumers than it should be. And we urge the Bureau to keep these facts in mind while it reviews the rule (to avoid changes that could unwittingly exacerbate the current situation further). But the evidence described above and other analysis in the Center for Responsible Lending's comments, show that the ATR/QM rule is not the source of this problem. Instead, credit tightening followed the crisis—not implementation of the ATR/QM rules. Ultimately, time, competition, and growing market confidence will continue to make more credit available. Weakening consumer protections will only help irresponsible lenders.

c. The QM rule does not appear to be affecting small loans.

One broadly-expressed area of concern about the QM rule is the impact on small balance loans. These loans historically have been more difficult to originate, given fixed costs and the industry's practice of basing compensation on a percentage of the loan balance. Critics have argued that the QM's limits on points and fees may have added to this difficulty, as it discourages charging more than a certain amount of points According to the Urban Institute's research[20], however, there is little evidence that the rule had a negative effect on the origination of smaller balance loans.

Small loans are important to borrowers with limited means or in weaker markets. These borrowers are often the most vulnerable because they have fewer options, less education, and less income. These factors can make them attractive targets for predators. Home improvement and repair loans in particular are often smaller than other mortgages and have a long history of abuse from door-to-door salesmen and hard-money lenders.

Because this community needs access to safe credit, we agree that the Bureau should continue to monitor the small-loan market. However, the QM rule already provides substantially higher caps for

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[20] *Has the QM Rule Made it Harder to Get A Mortgage?,* Urban Institute, op. cit.

smaller loans (defined in 2017 as those under $102,894). Only if there is clear evidence that the rule is artificially reducing lenders' willingness to extend credit should the Bureau consider changing the caps. But any adjustment to the points-and-fees threshold should be based on the fixed costs of origination and actual risk, not simply perceptions regarding liability for non-QM loans.

One lender trade group has recommended that the more generous points and fees cap be extended as far as $200,000. Such a proposal is based on the average loan amount today, which is $260,000.[21] We do not support a change that would weaken the points and fees cap to include such a large portion of all mortgage loans. The Bureau's plan includes further review along with information gathering from lenders. We believe such a review is appropriate, and we look forward to the results of this research.

III. Land installment contracts: subject to the ability-to-repay rule but should be ineligible for qualified mortgage status

Land contracts are essentially a form of seller financing in which legal title remains in the seller's name until all payments have been made. This type of contract is often described to low-income people as a way to acquire homeownership without needing to deal with a bank or get credit approval. But they subject buyers to considerably more risk than traditional mortgages because of the long delay in transferring legal title and other abusive features.[22]

The CFPB should clearly state what is already true and not legitimately disputed: that these arrangements are covered by the Truth in Lending Act and subject to the ability-to-repay requirements. But, due to their inherently risky features, the Bureau should amend Regulation Z to explicitly exclude land installment contracts from the definition of a Qualified Mortgage.

A. Land installment contracts are unfair and abusive by

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[21] Mortgage Bankers Association, *ATR/QM Improvements*, *available at* https://www.mba.org/issues/residential-issues/atr/qm-improvements.

[22] *See* Heather K. Way & Lucy Wood, *Contracts for Deed: Charting Risks and New Paths for Advocacy*, 23 J. Affordable Hous. & Cmty. Dev. L. 37 (2014).

design and often target underserved populations, including communities of color.

Land installment contracts are also known as contracts for deed, bond for deed or bond for title, installment sale contracts, long-term land contracts, and land sale contracts. Here we refer to them as "land contracts" or "land installment contracts." In this discussion, the term "seller" will be used to refer to the non-consumer party to the land installment contract and "buyer" will be used to refer to the consumer. These labels recognize the reality that most land installment contracts involve the sale of real property.

Sometimes, however, land installment contracts are used for purposes other than the initial purchase of the property. For example, some transactions involve foreclosure rescue scams in which the "buyer" already owns the home and transfers the deed to the "seller" in exchange for the seller paying off mortgages on the house.[23] Occasionally, a seller may refinance an existing land installment contract, to reflect altered payment terms, the addition of taxes or repair costs to the balance, or (rarely) as part of the transfer of legal title in the property.

Because in many jurisdictions land installment contracts are subject to very little regulation, land contracts are often synonymous with overpriced credit on dilapidated homes. Land contracts flourish in areas underserved by conventional lenders and with buyers who lack access to credit.[24] Sometimes the lack of access to credit results in benign land installment contracts, such as in rural areas, where contracts between farmers are often arms-length transactions. But all too often land installment contracts have flourished in inner cities and impoverished areas where a legacy of racial discrimination and

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[23] *See* National Consumer Law Center, Foreclosures and Mortgage Servicing Ch. 18 (5th ed. 2014), *updated at* www.nclc.org/library (discussing foreclosure rescue scams).

[24] Jeremiah Battle, Jr., Sarah Mancini, Margot Saunders, & Odette Williams, National Consumer Law Center, Toxic Transactions: Land Installment Contracts Once Again Threaten Communities of Color (July 2016), *available at* https://www.nclc.org/issues/toxic-transactions-threaten-communities-of-color.html.

redlining by lenders have left communities starved for credit.[25] In these cases, sellers have exploited that legacy to strip wealth from communities.[26]

Sellers may prolong land installment contracts indefinitely—making homeownership and equity acquisition a mirage—by tacking other fees onto the contracts or by misapplying payments. As a result, the contract price steadily increases even when payments are made on time.[27] Or sellers may never intend to complete the sale—using land installment contracts as a method of renting property while evading a landlord's normal duties to make repairs. When sellers use installment land contracts for rental arrangements, communities are doubly harmed. The overpriced credit robs the community of capital (in part, because sellers often demand an outsized down payment to maximize their profit) and the local housing stock steadily deteriorates.

Even in the absence of fraud, unfavorable contract terms coupled with the lack of protections in the common law can make these deals problematic for consumers unable to seek legal advice before signing the contract.

As a result of the foreclosure crisis that began in 2007, many former homeowners have damaged credit histories and cannot purchase another home through traditional mortgage lenders. These former homeowners may respond to land installment contract sellers who offer homes at seemingly affordable prices despite the prospective homeowners' poor credit histories.[28] Some home seekers actually may

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[25] *Id*. *See, e.g.*, David Migoya, *Denied Loan at Bank, Buyers Have Few Options*, Belleville News-Democrat, May 18, 1993, at A1.

[26] *See, e.g.*, Clark v. Universal Builders, Inc., 501 F.2d 324 (7th Cir. 1974) (finding complaint adequately alleged that sellers took advantage of dual housing market to demand prices and terms from black buyers unreasonably exceeding those available to white buyers of equivalent housing).

[27] *See, e.g.*, David Migoya, *Homebuyers' Dreams Fade*, Belleville News-Democrat, May 16, 1993, at 1A (documenting that a majority of buyers in the East St. Louis area had steadily increasing balances on their contracts).

[28] Jeffrey Meitrodt, Contract for Deed Can Be House of Horror for Buyers, Star Tribune, Jan. 14, 2013, *available at* www.startribune.com (contract for deed sales in the Minneapolis area increased more than 50% in the past five years attracting families with low incomes or damaged credit; actual number of these transactions is "vastly underestimated" because the contracts are

believe they are signing a lease, not a sales contract.[29] Property flipping companies are buying up properties cheaply at foreclosure sales or from lenders' post-sale inventories, such as those of Fannie Mae or Freddie Mac, and subsequently selling the homes using land installment contracts.[30] These properties may be in poor shape and often suffer from lead paint and other hazards.[31]

B. Land installment contracts are covered by the Truth in Lending Act.

Land installment contracts are already covered by the Truth in Lending Act. But the Bureau should make this explicit by formally clarifying that land installment contracts are credit and are residential mortgage loans. Issuing such a clarification will simply formalize in the regulations the conclusion obviously derived from the Bureau's investigation of Harbour Portfolio.[32] A formal clarification will encourage sellers to begin using the proper disclosures and to obey the ability-to-repay rule. And if they fail to do so, it will alert consumers directly to the tools they need to protect themselves against known fraud and abuse in this area.

1. Land installment contracts are credit that often is provided by a creditor.

TILA, including its disclosure requirements, applies to land installment contracts if the seller meets the definition of a creditor and if the contract is offered primarily for personal, family, or household

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not recorded).

[29] *Id.*

[30] Heather Perlberg, *Apollo's Push into Business that Others Call Predatory*, Bloomberg, Apr. 7, 2016, *available at* www.bloomberg.com; Alexandra Stevenson & Matthew Goldstein, *Market for Fixer-Uppers Traps Low-Income Buyers*, The New York Times, Feb. 21, 2016, at A1.

[31] *See, e.g.*, Rush v. Vision Prop. Mgmt., L.L.C., No. 27CV 12-22357 (Minn. Dist. Ct. Apr. 18, 2013) (order) (describing a property flipping scheme that included selling the homes using contracts for deed).

[32] Consumer Financial Protection Bureau v. Harbour Portfolio, 2017 WL 631914 (E.D. Mich. Feb. 16, 2017) (stating that Harbour contracts appeared to be credit "because they obligate the purchaser to pay a principal sum plus interest through deferred monthly payments").

purposes.[33] Generally a land installment contract is "credit" because it creates a debt (the purchase price) and defers its payment or because the contract defers payment of debt (the purchase price).[34] The seller meets the definition of a creditor if he or she is a person who "regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments (not including the down payment) and to whom the obligation is initially payable."[35] The land installment contract usually requires the buyer to make more than four payments or requires the payment of interest or both. In 2017, a federal district court upheld the Consumer Financial Protection Bureau's jurisdiction to demand documents and information from Harbour Portfolio, a contract for deed seller, stating that the contracts appear to involve an extension of credit for purposes of TILA.[36]

Whether the seller "regularly extends" consumer credit is a numerical test. The general rule is that this test is met if the seller entered into more than twenty-five consumer credit transactions in the preceding calendar year.[37] However, a seller that entered into as few as six consumer credit transactions in the preceding year will meet the numerical test if those transactions were secured by a dwelling.[38] And, the threshold is lower still for HOEPA loans: a seller that originates

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[33] Reg. Z, 12 C.F.R. § 1026.2(a)(12) (definition of "consumer credit"). *See also* National Consumer Law Center, Truth in Lending § 2.5.5 (9th ed. 2015), *updated at* www.nclc.org/library.

[34] Reg. Z, 12 C.F.R. § 1026.2(a)(14) (definition of "credit"). *See* National Consumer Law Center, Truth in Lending § 2.2 (9th ed. 2015), *updated at* www.nclc.org/library.

[35] Reg. Z, 12 C.F.R. § 1026(a)(17)(i) (definition of "creditor"). *See* National Consumer Law Center, Truth in Lending § 2.3 (9th ed. 2015), *updated at* www.nclc.org/library.

[36] Consumer Financial Protection Bureau v. Harbour Portfolio, 2017 WL 631914 (E.D. Mich. Feb. 16, 2017) (stating that, although Harbour's defense challenging TILA coverage was premature in any event, the Harbour contracts appeared to be credit "because they obligate the purchaser to pay a principal sum plus interest through deferred monthly payments").

[37] Reg. Z, 12 C.F.R. § 1026.2(a)(17)(v).

[38] Reg. Z, 12 C.F.R. § 1026.2(a)(17)(v). *See* National Consumer Law Center, Truth in Lending § 2.3.3 (9th ed. 2015), *updated at* www.nclc.org/library.

two or more HOEPA mortgages or one HOEPA mortgage through a broker is deemed to regularly extend credit.[39]

Whether the lower thresholds apply depends on whether the loans are secured by a "dwelling." The property being purchased under a land installment contract ordinarily meets the definition of a "dwelling."[40] The only question is whether the contract is *secured* by an interest in the dwelling under state law.

In the few cases in which the applicability of TILA's disclosure rules to land contracts was at issue, the courts appear to have assumed that there is no reason why, conceptually, land installment contracts would not constitute "consumer credit."[41] Rather, other than remanding to determine the facts supporting such an allegation, courts have focused on the numerical test.[42] The Act, Regulation Z, and the official interpretations also already assume that land installment contracts constitute credit.[43] The CFPB should make it clear in the official

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39 15 U.S.C. § 1602(g). Note that a land installment contract can be covered by HOEPA.

40 A dwelling is "a residential structure that contains one to four units." Reg. Z, 12 C.F.R. § 1026.2(a)(18). The definition thus excludes land installment contracts involving commercial property or residential property with more than four units.

41 *See* National Consumer Law Center, Truth in Lending § 2.5.5 (9th ed. 2015), *updated at* www.nclc.org/library.

42 Hodges v. Swafford, 863 N.E.2d 881, 886–888 (Ind. Ct. App. 2007) (ruling that an intermediary brokered the land contract, the transaction was covered by HOEPA and, consequently, the seller was a creditor because it met the one or more brokered loan threshold), *amended on other grounds*, 868 N.E.2d 1179 (Ind. Ct. App. 2007); Beltran v. Robert M. Anderson Trust, 210 F.Supp.3d 1105, 1109 (D. Minn. 2016) (material dispute of fact existed regarding number of transactions).

43 *See, e.g.*, 15 U.S.C. § 1602(x) (including "purchase money security interest under an installment sales contract" in the definition of "residential mortgage transaction"); Reg. Z, 12 C.F.R. § 1026.2(a)(24) (same); Official Interpretations, 12 C.F.R. § 1026.2(a)(24) (suggesting that a buyer can acquire an interest in a dwelling even if the consumer had not acquired full title). *Cf.* Official Interpretations, 12 C.F.R. § 1026.3(a)-10 (discussing under what circumstances credit extended for consumer purposes to a land trust constitutes "credit" even though the trust holds title to the property and the underlying loan note is executed by the trustee; stating that "in

interpretation that land installment contracts are "secured by" a dwelling in the Bureau's view, reflecting the true nature of these transactions as a mortgage substitute. Moreover, the Bureau should clearly state that land contract sellers may not evade TILA coverage by using multiple shell corporations.

Land contract sellers may claim that TILA does not apply to the transaction because there is no "extension of credit" since a buyer may terminate the contract at any time without penalty. However, this is simply not the case in a land installment contract. In these contracts, the buyer promises to pay the entire purchase price, and a debt is created by the deferral of that purchase price over a period of time. If the buyer defaults, the seller has the right to sue for breach of contract and specific performance, demanding the purchase price in full. The fact that the seller may, in the alternative, elect to rescind or forfeit the contract and recover the house in lieu of the debt makes no substantive difference. The buyer has no control over what remedy a seller elects. Thus, it cannot be said that the buyer has the ability to terminate the contract without penalty. In this way, land contracts are distinct from a lease with an option to purchase,[44] wherein the tenant may decide to walk away without exercising the option and avoid any further liability beyond the rent owed for the lease term.[45]

2. Land installment contracts are residential mortgage loans and are subject to the ability-to-repay requirement.

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substance (if not form) consumer credit is being extended.").

[44] *See* National Consumer Law Center, Truth in Lending § 12.2.2 (9th ed. 2015), *updated at* www.nclc.org/library (discussion of the differences between a lease with an option to buy and a land installment contract).

[45] *See* Johnson v. Washington, 559 F.3d 238 (4th Cir. 2009) (finding no TILA coverage because an "option" to repurchase is not equivalent to an "obligation" to repurchase, and therefore did not constitute a debt); Redic v. Gary H. Watts Realty Co., 762 F.2d 1181 (4th Cir. 1985) (finding defendants were not "creditors" for purposes of TILA because the transactions used to establish the numerical requirement were in fact sales with the option to repurchase).

The ability-to-repay rule applies to residential mortgage loans.[46] A residential mortgage loan is "any consumer credit transaction that is secured by a mortgage, deed of trust, or other equivalent consensual security interest on a dwelling."[47] Land contracts constitute a consensual security interest on a dwelling that is equivalent to a mortgage or deed of trust in those states that treat land installment contracts as mortgages.[48] In the other states, the result should still be the same due to the traditional meaning of the term "secured." *Black's Law Dictionary* defines "secured" as: "(Of a debt or obligation) supported or backed by security or collateral . . . (Of a creditor) protected by a pledge, mortgage, or other encumbrance of property that helps ensure financial soundness and confidence."[49] The *Restatement (Third) of Property (Mortgages)* describes a land installment contract as: "a contract for the purchase and sale of real estate under which the purchaser acquires the immediate right to possession of the real estate and the vendor defers delivery of a deed until a later time to *secure* all or part of the purchase price."[50]

A land installment contract is functionally equivalent to a seller's purchase money mortgage from an economic perspective. In comparing the two types of contracts, one professor wrote: "Both devices provide *security* for a seller of real estate who finances all or part of the purchase price."[51] As a court put it: "An installment land

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[46] While this discussion focuses only on the applicability of the ability-to-repay rule to Land Installment Contracts, coverage by TILA also likely results in application of other aspects of the regulations, including disclosures and the high-cost and higher-cost mortgage rules.

[47] 15 U.S.C. § 1602(cc)(5).

[48] Skendzel v. Marshall, 301 N.E.2d 641, 646 (Ind. 1973) ("[A land contract is] a sale with a security interest in the form of legal title reserved by the vendor. Conceptually, therefore, the retention of the title by the vendor is the same as reserving a lien or mortgage. Realistically, vendor-vendee should be viewed as mortgagee-mortgagor.").

[49] Black's Law Dictionary 1475 (9th ed. 2004). "Security" refers to "collateral given or pledged to guarantee the fulfillment of an obligation; esp., the assurance that a creditor will be repaid." *Id.*

[50] Restatement (Third) of Property (Mortgages) § 3.4(a) (1997) (emphasis added).

[51] Grant S. Nelson, *The Contract for Deed As a Mortgage: The Case for the Restatement Approach*, 1998 BYU L. Rev. 1111, 1112 (emphasis added).

sale contract is one of three *security* devices generally used in credit transactions in real estate and is, in essence, a hybrid composed of property law concepts on the one hand and contract law on the other."[52] Moreover, even if the obligation created in a land installment contract were not "secured by a dwelling," TILA would still apply, subject to the higher numerical threshold to qualify as a creditor in non-mortgage credit.

3. Land installment contracts should be excluded from the qualified mortgage definition and its presumption of affordability.

As the Bureau notes in its Request for Information, Congress enacted the ability-to-repay requirements for mortgages as part of the Dodd-Frank Act in response to historic expansion and contraction of the mortgage market. The rules provide for a class of "qualified mortgages" for which compliance with the ability-to-repay requirement is presumed. As the CFPB stated in a blog earlier this year, these are loans with "more stable features" that make it more likely a consumer can afford the loan.[53] Essentially, the Qualified Mortgage is intended to be a "plain vanilla" product that a borrower can assume will be safe.

Whether the loans come with a rebuttable or irrebuttable presumption of compliance, the Qualified Mortgage rule gives lenders significant insulation from liability. As a result, the Bureau has carved out certain products from the Qualified Mortgage category, including interest-only loans, negative amortization products, many balloon loans, and loans with terms longer than 30 years. These are products that are inherently riskier than those allowed to have Qualified Mortgage status.

Land installment contracts also have a significant inherent degree of risk and should, therefore, be barred from having Qualified

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[52] Ellis v. Butterfield, 570 P.2d 1334, 1336 (Idaho 1977) (emphasis added). *See also* Lyons v. Pitts, 923 So. 2d 962, 965–966 (La. Ct. App. 2006) (the bond for deed is used as a security device in favor of the seller).

[53] Consumer Financial Protection Bureau, "What is a Qualified Mortgage" (Feb. 22, 2017), *available at* https://www.consumerfinance.gov/ask-cfpb/what-is-a-qualified-mortgage-en-1789/.

Mortgage status. These loans are, by their very structure, likely to result in default, akin to the negative amortization and interest-only products already barred. They also are unlikely to result in the accrual of significant home equity, similar to the loans barred from the Qualified Mortgage status because their terms exceed 30 years. Like balloon loans and the interest-only/negative amortization products currently excluded from QM, land contracts can result in an elevated risk of loss of the consumer's home. Whereas interest-only and negative amortization products create that risk through the likelihood of a sharp payment shock, land contracts do so through the structure of the transaction involving a forfeiture clause—which puts the would-be homeowner into a swift dispossessory process, often with no chance of recovery.

IV. The QM patch has worked and should be maintained.

In the current QM rule, the Bureau tries to strike a balance between creditors' desire for a "bright line" (to identify QM loans) and maintaining broad access to responsible credit. Adopting the 43-percent debt-to-income (DTI) ratio satisfied the first but potentially complicated the second. The so-called "patch" ameliorated this problem. During the rulemaking, some expressed concern about having any single factor, such as DTI ratio, serve as essentially the sole means of measuring ability to repay. The Bureau ultimately chose the additional option to grant QM status to loans that were accepted for delivery to Fannie Mae, Freddie Mac and other government mortgage insurance programs, which use compensating factors. This so-called "patch" was limited to seven years or the end of the conservatorship of Fannie and Freddie that began in 2008. But this patch has become the standard means by which creditors determine QM eligibility. We support its continued use unless and until the Bureau develops a standard that more effectively balances the need for a bright line with reasonable credit underwriting balancing multiple factors that have a statistically valid relevance to determining a consumer's likely ability to repay. We also encourage the Bureau to explore whether the patch has any discrete effects on the various borrower populations it is examining more closely, such as LMI borrowers and borrowers of color.

Another proposal raised during the initial rulemaking but also not adopted was requiring use of residual income or residual income standards to supplement or replace the DTI standard. Residual income is an important measure of affordability, particularly for borrowers at the lower end of the income spectrum, where DTI may not be adequately reflective of monthly cash availability.[54] CFA has recently begun a new research project to model a residual income test that could be considered in the broader mortgage underwriting and specific QM context. We look forward to sharing the results of this work, hopefully before the end of 2017. We also encourage the Bureau to work on this topic with other agencies to help develop alternative measures of affordability.

Under the current rule, the patch applies to loans approved for delivery by Fannie, Freddie, FHA, VA, and RHS. These federal credit insurers have issued their own QM definitions which differ somewhat from the Bureau's rules that apply to the GSEs. While we support the patch, the Bureau needs to more closely examine whether it is appropriate to have varying standards for the rule depending on the source of credit insurance that the loan has. In other words, GSE loans carrying private mortgage insurance are subject to one set of requirements (outside of underwriting standards), but those insured by the FHA have slightly different requirements. If the purpose of the ATR test is to assure that the lender has made the required reasonable determination, it is not clear why this should vary based on the source of credit enhancement. On the other hand, we want to ensure that FHA and VA borrowers maintain their access to the market even where their borrower profiles may differ from GSE borrowers.

We reiterate that the purpose of the ATR rule is to ensure that creditors fully understand and evaluate a consumer's ability to repay a loan on the terms at which it is offered. Although we support a standard that does not unreasonably constrain credit, we also strongly oppose changes that could enable creditors to repeat past mistakes by offering credit on terms that fail to meet this important test.

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[54] Michael Stone, *What is Housing Affordability? The case for the Residual Income Approach* , Housing Policy Debate, Vol. 17, Issue 1 (Aug. 31, 2006), *available at* https://works.bepress.com/michael_stone/5/.

V. Appendix Q should be reevaluated.

The ATR/QM rule added Appendix Q to Regulation Z. Appendix Q contains underwriting guidance for creditors seeking to make QM loans on applications that do not fit a standardized model. This guidance is helpful because it supports granting credit to borrowers who cannot benefit from the QM "patch" without further documentation.

Nevertheless, conversations with lenders serving these consumers has convinced us that there are better ways to accomplish the same goal. This kind of underwriting also may be part of the solution to expanding non-federally guaranteed, responsible credit.

As an example, Appendix Q requires significantly more documentation of self-employment income that supplements regular W-2 income than does the Fannie Mae Seller-Servicer Guide, including two years of tax returns, (both 1040's and K-1s where appropriate); year-to-date profit and loss figures; and year-to-date balance sheet for the self-employment venture. Fannie Mae requires only paystubs for the W-2 employment and a tax transcript to document self-employment income when it is not the borrower's primary source of income. Appendix Q's requirements for such significant documentation add time and expense to the mortgage application process, and can discourage both creditors and borrowers from pursuing loans when such income is present. The Fannie Mae rules still require documentation but in a significantly streamlined fashion.

The Bureau in its review should carefully review Appendix Q's utility and consider accepting the requirements of Fannie and Freddie's Seller Servicer Guides, as it has accepted their automated underwriting findings, or alternative requirements more in line with what the primary providers of mortgage credit today accept as a means through which lenders can meet the QM test. The Bureau should examine any differential effect such adoption might have on special categories of borrowers, including the self-employed, seasonal workers, and low- and moderate-income borrowers.

VI. High-cost open-end credit should be subject to a more stringent ability-to-repay analysis.

Currently creditors may not make most closed-end loans without confirming that the borrower has the ability to repay the debt.[55] The Bureau decided that this rule, and the Qualified Mortgage presumption, should apply to high-cost closed-end loans too, even though HOEPA already includes an ability-to-repay rule, because the § 1026.43(c) rule better protects consumers:

> [A]lthough they are similar, the Bureau generally considers the ability to-repay requirements set forth in § 1026.43 to be more protective of consumers than the current ability-to-repay criteria for high-cost mortgages set forth in current § 1026.34(a)(4)(i)–(iv). . . . The Bureau generally believes these criteria to be more rigorous than the current ability-to-repay provisions.[56]

Yet, despite the importance of the stronger ability-to-repay rule, the rule excludes open-end lines of credit.[57] We strongly encourage the Bureau to rectify that gap. There is no justification for excluding HELOCs. The volume of dwelling-secured open-end credit is large enough to have a systemic importance to the economy.[58] And, from the borrower's perspective, when it is time to make the monthly payment, there is little functional difference between a fully-drawn HELOC and a closed-end loan.

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[55] Reg. Z § 1026.43(c).

[56] Fed. Reg.: 78 Fed. Reg. 6856, 6925 (Jan. 31, 2013).

[57] Reg. Z §§ 1026.43(a)(1) (excluding HELOCs from ATR rule); 1026.34(a)(4) (creditor shall not open high-cost HELOC "without regard to the consumer's repayment ability as of account opening").

[58] *See* CoreLogic, Home Equity Lending Landscape at 1 (Feb. 2016), *available at* https://www.corelogic.com/research/home-equity-lending-landscape/home-equity-lending-landscape.pdf (noting $364 billion of HELOC originations at peak in 2005 and rising originations in recent years, to $115.8 billion in 2015); New York Fed. Reserve, Quarterly Report on Household Debt and Credit (Feb. 2017) ("Balances on home equity lines of credit (HELOC) were roughly flat and now stand at $473 billion."). *See also* Jim DuPlessis, Credit Union Times Magazine, *Borrowing Shifts From Re-Fi to HELOC* (Jan. 20, 2017), available at http://www.cutimes.com/2017/01/20/borrowing-shifts-from-re-fi-to-heloc

For a borrower, the two most relevant features of either form of credit are that both provide funds to do something the borrower deems important, and both put the borrower's house on the line. The consequences of foreclosure for the borrower, the noteholder, and the economy do not depend on whether the loan is open- or closed-end. Therefore the standards for the ability-to-repay rule should not differ either.

VII. Additional Recommendations

We also have a number of other recommendations regarding Regulation Z and the Bureau's rule-assessment plan.

- The Bureau should closely examine and better regulate Property Assessed Clean Energy (PACE) loans. There are significant questions about whether this product is repeating the mistakes and abuses of the subprime lending industry. Despite industry claims to the contrary, PACE loans are credit[59] and should comply with the Truth in Lending Act.
- The Bureau should not expand QM status to portfolio loans held by larger institutions. How well a consumer is protected from predatory or unsafe lending should not depend on who owns the loan.
- The Bureau should not lift the points and fees triggers for lender-affiliated title insurance companies or higher loan amounts.
- The Bureau should preserve the rebuttable presumption for high-cost mortgages; and
- The small creditor exemptions should apply only to depository lenders.

We commend the Bureau on its rule-assessment plan, and we recommend the following regarding methodology:

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[59] National Consumer Law Center, *Truth in Lending* § 2.4.9.3 (9th ed. 2015) (*updated online at* https://library.nclc.org/). *See generally,* NCLC PACE analysis available at https://www.nclc.org/issues/pace-loans.html.

- Assess the affordability of current loans and model market performance under other market conditions in order to evaluate how well the rule prevents unaffordable lending and loan defaults;
- Build on existing approaches in assessing loan availability, including considering market conditions that might help explain observed changes;
- Consider the rule's effect on the overall financial system;
- When making the assessment, incorporate outreach to borrowers and consumer advocates; and
- Maintain the Bureau's plan to analyze the rule's differential impact, if any, on certain categories of borrowers, including: self-employed, those relying on assets, part-time and seasonal workers, those with smaller-than-average loan amounts, borrowers with debt-to-income ratios above 43%, low- and moderate-income borrowers, borrowers of color, and rural borrowers.

We would be happy to meet with the Bureau to discuss any of these recommendations in greater detail.