| **HIGHLIGHTS OF PROPOSED ABILITY-TO-REPAY RULES** | | |
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| The proposal under Regulation Z would require creditors to determine a consumer's ability to repay a mortgage before making the loan and establish minimum mortgage underwriting standards. The revisions to the regulation, which implements the Truth in Lending Act (TILA), are being made pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or Act). * | | |
| **SCOPE** | Consistent with the act, the proposal would apply the ability-to-repay requirement to all consumer-purpose mortgages (except home equity lines of credit, timeshare plans, reverse mortgages, or temporary loans). | |
| **COMPLIANCE OPTIONS** | | |
| **OPTION # 1**<br><br>**GENERAL ABILITY-TO-REPAY STANDARD** | Considering and verifying eight (8) underwriting factors: | (1) Income or assets relied upon in making the ability-to-repay determination |
| | | (2) Current employment status |
| | | (3) The monthly payment on the mortgage |
| | | (4) The monthly payment on any simultaneous mortgage |
| | | (5) The monthly payment for mortgage-related obligations |
| | | (6)Current debt obligations |
| | | (7)The monthly debt-to-income ratio, or residual income |
| | | (8) Credit history |
| | Underwriting the payment for an adjustable-rate mortgage based on the fully indexed rate. | |
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| **OPTION # 2**<br><br>**QUALIFIED MORTGAGE** | A creditor can originate a "qualified mortgage," which provides special protection from liability. The FRB is soliciting comment on two alternative definitions of a "qualified mortgage." | |
| **Alternative 1** | | |
| Alternative 1 would operate as a legal safe harbor and define a "qualified mortgage" as a mortgage for which: | | The loan does not contain negative amortization, interest-only payments, or a balloon payment, or a loan term exceeding 30 years. |
| | | The total points and fees do not exceed 3 percent of the total loan amount. |
| | | The income or assets relied upon in making the ability-to-repay determination are considered and verified. |
| | | The underwriting of the mortgage (1) is based on the maximum interest rate that may apply in the first five years, (2) uses a payment scheduled that fully amortizes the loan over the loan term, and (3) takes into account any mortgage-related obligations. |
| **Alternative 2** | | |
| Alternative 2 would provide a rebuttable presumption of compliance and would define a "qualified mortgage" as including the criteria listed under Alternative 1 as well as additional underwriting requirements from the general ability-to-repay standard. | | Consumer's employment status. |
| | | The monthly payment for any simultaneous mortgage. |
| | | Consumer's current debt obligations. |
| | | The monthly debt-to-income ratio or residual income. |
| Thus, under Alternative 2, the creditor would also have to consider and verify: | | Consumer's credit history. |

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| **Option # 3**<br><br>**Balloon-Payment Qualified Mortgage** | A creditor operating predominantly in rural or underserved areas can originate a balloon-payment qualified mortgage. This option is meant to preserve access to credit for consumers located in rural or underserved areas where creditors may originate balloon loans to hedge against interest rate risk for loans held in portfolio. | |
| | Under this option, a creditor can make a balloon-payment qualified mortgage with a loan term of five years or more by: | Complying with the requirements for a qualified mortgage. |
| | | Underwriting the mortgage based on the scheduled payment, except for the balloon payment. |
| **Option # 4**<br><br>**Refinancing of a Non-Standard Mortgage** | A creditor can refinance a "non-standard mortgage" with risky features into a more stable "standard mortgage." This option is meant to preserve consumers' access to streamlined refinances that materially lower their payments. | |
| | Under this option, a creditor complies by: | Refinancing the consumer into a "standard mortgage" that has limits on loan fees and that does not contain certain features such as negative amortization, interest-only payments, or a balloon payment. |
| | | Considering and verifying the underwriting factors listed in the general ability-to-repay standard, except the requirement to consider and verify the consumer's income or assets. |
| | | Underwriting the "standard mortgage" based on the maximum interest rate that can apply in the first five years. |
| | **Other Features** | |
| **Other Protections** | The proposal would also: | Implement the Dodd-Frank Act's limits on prepayment penalties. |
| | | Lengthen the time creditors must retain records that evidence compliance with the ability-to-repay and prepayment penalty provisions. |
| | | Prohibit evasion of the rule by structuring a closed-end extension of credit as an open-end plan. |
| * **Rulemaking Process** | On July 21, 2011, the FRB transferred general rulemaking authority for TILA to the Consumer Financial Protection Bureau (CFPB).<br><br>Accordingly, this rulemaking will be finalized by the CFPB. | |