Agencies on the QM/QRM

I am responding to the invitation on page 271 to comment on all aspects on the proposal to equate QRM with QM.

I believe this is a grave error, and contrary to the assertion that it would best carry out the statutory intent, significantly repudiates it. Readers of the proposal will have a very hard time understanding why Congress would have created two separate categories, in two separate parts of the statute, if it intended they would be treated identically.

The statutory intent was to create 3 categories of mortgages: those that fell below QM standards and were subject to various legal constraints; the QM mortgages which would meet minimum standards and be subject to risk retention; and a separate sub-set of mortgages that were virtually certain to be repaid and would therefore be given an exemption from risk retention.

The agency's main proposal renders the concept of an "exemption" from

risk retention meaningless. The result would be two categories-those that fell below standards and probably shouldn't be made, and those that could be made and would not be subject to risk retention.

I am reinforced in the view that regulating the concept of risk retention out of the statute and out of the mortgage business is a mistake by the proposals acknowledgement "that the direct costs incurred by a sponsor for funding the retain portion should be small." The citation of "plausible estimates" that the additional cost would range from "0-30 basis point" argues for some category of mortgages being subject to risk retention, given the agencies acknowledgement that this does incentivize better practices. I am wholly unpersuaded by the agency's then citing "indirect cost" as a reason for regulating risk retention out of existence, especially since the proposal concedes that these are "difficult to quantify", even though in what frankly appears to be a reach for cover, the document does

say that they “have the potential to be large.” Reference to unquantifiable costs suggests that there are people who don’t like risk retention and are looking for a way to justify its de facto abolition. Adding that they “have potential to be large” adds no weight to the proposal. Many things have the “potential” to be large; public policy should be grounded in what is likely, not what is merely possible.

I am not surprised that, as noted on page 278, the overwhelming majority of commenters who are interested in building, selling or promoting the sale of housing to lower income people, support effectively abolishing risk retention I should note that if all of these people were correct in their collective judgment, we would not have had the crisis that we had. More importantly, what their arguments reflect, and what I believe unfortunately is carried over in proposal, is the view that things must always be exactly as they are today, I understand that since risk retention is a new concept,

people in various phases of the business of housing are unused to it, and do not like the changes it will force in their operation. But the very purpose of the statute was in fact to bring about changes in a number of areas in our financial life, residential mortgages foremost among them.

Nothing in the agency's discussion-nor our experience-demonstrates that the people in this business are incapable of adjusting to a rule whose genesis was the reality of unwise mortgages that resulted from the ability to do 100% securitizations. This is especially true if loans made under the new rules set forth for mortgages are in fact as safe as they should be. Retaining the risk of mortgages that are highly likely to be paid in full over time is likely not to cost very much.

I am particularly troubled by the notion that QM/QRM should be merged. The statue calls for three classes of mortgages rather than the two that are effectively represented in the agency's proposal. The logic of the statute

dictates that we retain the ability to treat these two categories of mortgages as distinct.

I earlier expressed my opposition to a flat 20% down payment requirement, I continue to believe that that is too rigid, but I also believe that the level of down payment and other factors, including loan to value, have a role to play in distinguishing between QM and QRM.

Finally, it is relevant to note that recent unrebutted newspaper reports demonstrate that the credit rating agencies which were so much a part of the problem in the past are reverting to those dangerous practices. That is, any notion that we can rely on the credit rating agencies to substitute for risk retention incentivizes good mortgage practices has no more justification than it did before. Those of us working on the legislation were eager to find ways to correct the credit rating agencies behavior, but I also confess that we were not very successful in doing that.

In summary, nothing in the discussion of the agency's proposal leads me to reconsider the views that I had when we drafted the legislation-mainly that we should have three categories of mortgages, not two, and that risk retention should be the rule, and 100% securitization the exception, only to be granted for mortgages far above the norm on the safety scale.