QRMs, MIDs & the housing market

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Most residents of Hollywood are very aware of the housing market correction (or crash, depending upon whom you ask) and are watching housing prices closely. We have received many questions about "the bottom" and when our mega buyer's market will again allow a seller to collect gains on a sale around here. Oddly, what we are not hearing much about is the current debate in congress about QRM and MID, both of which will certainly affect recovery of the housing market.

Ah! More acronyms?

The Mortgage Interest Deduction (MID) has been a part of our national tax code in varying forms since 1913, facilitating home ownership by reducing the carrying costs of owning a home. Simply stated, a homeowner can deduct mortgage interest paid. This tax incentive is one of the deductions that a deficit-focused Congress is considering scaling back or eliminating completely for certain tax brackets.

The Obama administration wants to reduce the MID for households making more than $250,000, estimating a $318 billion gain from such a change over the next 10 years. But Congress is not so sure, and it's now a hotly debated topic in Washington.

The more hotly debated, and perhaps higher-stakes issue, is a proposed change related to QRMs, Qualified Residential Mortgages. A banking reform rule proposed by the FDIC and Federal Reserve in April of this year would require a 20 percent minimum down payment on residential mortgage loans in addition to other criteria. Regulators maintain that higher down payment loans perform better than lower ones. It stands to reason. But some mortgage industry studies also show a minimal difference in exchange for a potentially big loss of sales.

The main issue for dissenters is the timing and end-costs of such a change. Raising a 20 percent down payment is a challenge for even many highly qualified buyers in today's economy. Since much lower down payments are available to qualified buyers and the housing market remains sluggish, the concern is that higher down payments would prompt more home-sales slowdown in an economy whose own recovery hinges significantly on housing's recovery.

Other QRM rules, from credit worthiness to income requirements, have widespread support as common-sense lending practices that align with the original intent of the Dodd-Frank Act for bank reform. But when the FDIC and Federal Reserve came out with this add-on, conflict arose.

According to the proposed definition, QRM borrowers would have to:

• Put at least 20 percent down to buy a home, have at least 25 percent in equity to refinance, have at least 30 percent in equity for a cash-out refinance.

• Have house payments that don't exceed 28 percent of before-tax income, and total monthly debt payments (house, credit cards, auto, student loans) couldn't exceed 36 percent of before-tax income.

• Not have been 60 days delinquent on any debt payments in the last two years.

John Campbell R-Calif., along with U.S. Rep. Brad Sherman, D-Calif., drafted a heavily supported letter that says the current version of the QRM would price creditworthy first-time and minority buyers out of the market.

According to the National Association of Realtors (NAR), 60 percent of recent home buyers made less than a 20 percent down payment. CoreLogic (the contractor that performed statistical analysis for Congress on the issue) says 39 percent of home buyers in 2010 made a down payment of less than 20 percent. Other studies put the number somewhere in between. In any event, many of those loans would not have passed muster under QRM rules.

The Center for Responsible Lending says, based on average home prices, it would take 14 years for the typical American family to save enough money for a 20 percent down payment, longer for high-cost areas like California. But even if the QRM down payment was lowered to 10 percent, as some suggest, one in four homebuyers could still be priced out of the market based on the nearly 25 percent of home buyers in 2010 who paid less than 10 percent down, according to CoreLogic.

It may be all moot.

Credit rating agency DBRS said underwriting standards today already simulate QRMs. According to DBRS, today's prime borrowers often must have an 80 percent loan-to-value ratio, a credit score of 680 to 720, two years' worth of W-2 forms and re-verification of employment within 10 days of closing the loan.

No matter which side of the debate you find yourself on, we can definitely all agree that the days of no credit check, no money down, interest-only mortgage loans are long gone. Good riddance. Qualified buyers will take good care of their homes and make better neighbors for all of us.

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