

Non-QM Lending

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Disclaimer

These statements are solely my opinions based on 44 years of mortgage finance experience and recent Non-QM research.

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Non-QM Trends

Agenda

- 1) Non-QM Risks
- 2) Non-QM: “A Paper” vs “Sub-Prime”
- 3) How to Identify a Wolf in Sheep’s Clothing
- 4) The New Subprime Aggregators
- 5) New Entrants

Non-QM Trends

Agenda

- 6) Funding Non-QM Loans
- 7) Legal and Regulatory Issues of Sub-Prime, Low Doc & No Doc Loans
- 8) Lending Reps & Warrants
- 9) To Lend Non-QM or Not

Non QM Risks

Penalty for Violating QM:

- 1) 3 Years Financing Charges
- 2) All Fees Paid at Closing
- 3) Legal Fees
- 4) Regulatory Fines (unspecified- no limit?)

Industry Estimate of Cost of Violation:

- 1) \$100,000 on Average Loan
- 2) \$200,000 on Jumbo Loans

The Big Unknown:

No Judicial Case-law or Precedent

Unknown Non-QM Risks

Reputational Risk: \$\$\$

Regulatory Risk: Unknown \$\$\$

Legal Risk: Unknown \$\$\$

Fraud & Misrep Repurchase Risk: \$\$\$UPB:

Proceed With Extreme Caution

The New Near Prime

- 1) Non-QM is not intended to fill the Sub-Prime Niche.
- 2) Sub-Prime is the same as 30 years ago- poor credit borrowers.
We simply have a easier way to identify it- FICO Scores.
- 3) Existing Lenders & new players are again pushing the credit envelop.
- 4) Believe it or not, SIVA, SISA, & NINA programs coming are back.

Wolf in Sheep's Clothing

- 1) FICO down to 500 & No FICO loans. “How low will you go?”
- 2) Max LTV of 60-80% (depending on the FICO score).
- 3) High Fixed Interest Rate: 3% - 9.5% above “A Paper” rates.
 - Low Doc = 5.5% - 8% rates.
 - Sub-Prime = 6% - 10% rates.
 - Low Doc Sub-Prime = 8 ¼% - 13% rates.
- 4) Origination Points = The More the Better- Whatever the Market Will Bear.
 - Thank God 3% Points & Fees Cap Only Applies to QM Loans!
- 5) Low/No Doc = Liar Loans

Liar Loan 3-peat

1980's: Liar Loans:” “No VOE/No VOD” loans-offered by Fannie & Freddie. Imploded in 1990-91 Recession- defense, hi-tech, & construction sectors all crashed at the same time. So much for industry diversification!

2000-2007: SIVA, SISA, NINA offered by all of the PMBS Issuers on Wall Street. Credit Meltdown. So much for geographic diversification!

2016: the return of Low/No Doc under Non-QM. Look Out!

Liar Loans: 60%- 70% of the stated incomes were inflated by 60-90%. Why else would you pay 6 5/8% - 13% rates in a 4% market?

Everyone makes money, til the Sun stopped shining!

Low/No Doc Loans

Low/No Doc is back for the 3rd Time in 30 Years

2016 Liar Loans: SIVA, SISA & NINA Loans.

New (OLD) Product Names:

Alternative Documentation Loans

Portfolio Programs

Alternative-Income Verification Loans

Asset-Based Loans

No Ratio Loans.

Lenders: Mostly mortgage companies, a few banks, & new shadow bankers.

Sound familiar?

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Top Stated Income Lenders

Scotsman Guide List of The Top Stated Income Lenders

Augora Hills Financial
AssetAvenue, Equity Secured Capital
Fidelity Mortgage Lenders Inc.
HML Investments
Home Bank of California
Kennedy Funding Financial
Pacific Private Money Loans
Riverdale Funding LL
South End Capital Corp
Velocity Mortgage Capital
Wilshire Finance Partners Inc.

Lenders & Brokers exceed 200 nationwide plus numerous Community Banks

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Non-QM Securitization

Liquidity is the key.

Non-QM PMBS Volume: \$54.1 billion issued in 2014. \$61.6 billion issued in 2015 vs. \$1.19 trillion issued in 2005

Most PMBS were re-securitization of 2000-2007 PMBS loans & new Jumbo Loans. Most Jumbo loans & IO's are kept in Bank portfolios.

Will the PMBS Market accept Sub-Prime Loans? Yes. Based on demand for yield.

Liar Loans? Not yet. How do you price in the Regulatory & Legal Risks?

There is no rated PMBS issuance for Liar Loans.

Wall Street is Back in the Game

Neuberger Berman
Pacific Investment Management Co
Blackstone Group Affiliate

...are lobbying Lenders to make more of these Alt-A loans or even buying loan origination companies to control more of the supplies themselves” (WSJ 2/2/16).

Will S&P and Moody’s get it right this time?

Who will perform the “due dili” on these Alt A (Low/No Doc) loans?
Alta A? These loans are really Alt F for FRAUD!

Non-QM Funding

Sub-Prime Loans: Wall Street issues rated PMBS sold to the broad investment community.

Alt A Low/No Doc Loans: sold to Private Equity Firms, Hedge Funds, & Mutual Funds.

1-4 Unit Investment Property Loans: Pooled into CMBS's.

NOO loans are commercial loans are not subject to QM.

Note: Occupancy misrep subjects that loan to Non-QM risk, litigation, Regulatory Enforcement & Repurchase (Fraud R&W's).

Bank Portfolios: mostly funds Non-QM I-O's and Non-QM loans for the Self-Employed & Immigrant population- foreign nationals.

Non-QM Legal/Regulatory Issues

Foreclosure & Class Action Issues: Pick your poison.

1) **UDAPP-** “I was deceived & misled”. No one explained it to me.

2) **Predatory Lending-** Who pays 6% to 13% rates when FHA offers FICO down to 580 & 3% cash down? Better to deny a loan.

3) **Steering-** to a higher cost loan or to a high cost loan that should have been denied.

4) **SARS-** If you do not verify assets, how can Brokers and Lenders Comply?

5) **Stated Income and/or Stated Assets-** facilitates FRAUD, a reportable felony.

Non-QM Legal/Regulatory Issues

6) **ATR Risks-**

DTI- Capacity to repay. Remember 25/25, 28/36, 33/38 and FHA 41% U/W Ratios?

Credit Worthiness- Willingness & demonstrated ability to repay.

7) **Fair Lending Disparate Impact-** Protected Classes

8) **IRS Liens-** for self-employed income & payroll tax avoidance precedes 1st Lien.

9) **Repurchase Risk-** 30 year risk on a 30 year loan.

Courts & Case Law do not recognize the 6 year statute of limitations on the 2000-2007era loan production, extending repurchase risk time-lines.

10) **Federal & State Regulators, Investors, and Plaintiff Bar will prevail in the end!**

To Lend Non-QM or Not

What should I do?

- 1) Always strive to do the right thing and put your customers interests before your own.
- 2) Establish & follow sound credit policies.
- 3) Not every borrower is qualified or ready for the mortgage obligation.
- 4) Be honest: intentional misrep is Fraud do not facilitate fraud.
- 5) Remember, fraud is a reportable felony & a Federal crime
- 6) The risks exceeds the rewards: Focus on I-Os & serving your bank customers.
- 7) Just say “NO” to SIVA, SISA, & Sub-Prime Loans.

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QM vs Non-QM

MBBA-NH New Products Sub-Committee

Watch List:

SIVA Loans

SISA Loans

NINA Loans

Sub-Prime Loans

Growing Equity Loan- Settlers Finance, LLC

(Contact Ben for details)

Wealth Building Home Loan- American Enterprise Institute

QM vs Non-QM

Questions?

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