

**American Bankers Association
American Financial Services Association
Consumer Bankers Association
Consumer Mortgage Coalition
Mortgage Bankers Association**

August 29, 2008

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th St. and Constitution Ave, NW
Washington, DC 20551
regs.comments@federalreserve.gov

Re: Docket No. R-1321

Dear Ms. Johnson:

The undersigned trade associations representing mortgage lenders and service-providers—the American Bankers Association,¹ the American Financial Services Association,² the Consumer Bankers Association,³ the Consumer Mortgage Coalition,⁴ and the Mortgage Bankers Association⁵ (collectively, the Associations)—appreciate the opportunity to submit comments on

¹ The American Bankers Association (ABA) brings together banks of all sizes and charters into one association that works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than \$125 million in assets – represent over 95 percent of the industry's \$13.3 trillion in assets and employ over two million men and women.

² The American Financial Services Association (AFSA) is the national trade association for the consumer credit industry protecting access to credit and consumer choice. The association encourages and maintains ethical business practices and supports financial education for consumers of all ages. AFSA has provided services to its members for over ninety years. AFSA's officers, board, and staff are dedicated to continuing this legacy of commitment through the addition of new members and programs, and increasing the quality of existing services.

³ The Consumer Bankers Association (CBA) is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services, community development, investments, deposits and delivery. CBA was founded in 1919 and provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets.

⁴ The Consumer Mortgage Coalition (CMC) is the trade association of national mortgage lenders, servicers, and service providers. Its members originate, service, and provide mortgage services to over 70% of the United States mortgage market.

⁵ The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 370,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's

the Board of Governors of the Federal Reserve System's (Board) proposed amendments (the Proposal) to the rules for reporting pricing information for higher-priced loans under the Home Mortgage Disclosure Act (HMDA). The Associations have been working together with their members in analyzing the Proposal and providing these comments.

Summary

- **We support use of a mortgage-based index as the benchmark for rate-reporting and conformance of the HMDA and HOEPA triggers.**

The Associations strongly support the shift in the benchmark for rate-reporting from Treasury securities to a mortgage-based index, the Freddie Mac Primary Mortgage Market Survey® (PMMS). This change will help reduce the variation in reported rate information that has resulted from changes in the financial markets rather than changes in mortgage lending patterns. We also strongly support making HMDA reporting thresholds and Home Ownership and Equity Protection Act (HOEPA) thresholds for coverage of loans as “higher-priced mortgage loans” correspond exactly, which will significantly ease the burden of compliance. We appreciate the Board's willingness to take on the burden of calculating the precise thresholds for rate-reportable loans. The Board's willingness to provide the industry with formal and precise numbers is crucial to providing lenders the assurance that they are in full compliance with these trigger requirements.

- **We recommend adjusting the benchmarks for particular market segments, including jumbo loans, loans with mortgage insurance, and FHA loans.**

At the same time, it is essential that the Board make further adjustments to the benchmark for particular segments of the market, including jumbo and insured or guaranteed loans, to assure that the benchmark accurately estimates the average prime rate and does not improperly classify mortgages as “higher priced” in those segments of the market. Without such adjustments, not only will HMDA data misclassify loans as “higher priced” but prime loans will be treated as subprime loans under the HOEPA rules. Applying the new HOEPA rules – and liability – to large segments of the prime market will decrease the availability and affordability of mortgages in these segments. Such an outcome would be contrary to the Board's well-considered determination to target greater protections under HOEPA to subprime loans while allowing the market to function with less restriction for prime loans.

Many if not most loans in market segments such as jumbo loans are demonstrably prime loans, and thus are not in the category of subprime loans, although it appears that many jumbo loans made at current rates would exceed the threshold for coverage under the Proposal. Others are government-insured or -guaranteed and subject to special protections for borrowers, while still

residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site:

www.mortgagebankers.org.

others are simply “higher-priced” because they include mortgage insurance costs. Accordingly, the Board should provide some simple adjustments to its proposed benchmarks for computing the rate spread for these market segments for which the PMMS does not produce an accurate estimate of the average prime rate. While we agree with the Board that it is important to seek simplicity in applying these new metrics, in this case modest refinements to the regulations would ensure that the Board achieves its goals without creating significant unintended consequences for major segments of the prime mortgage market.

- **The industry needs additional time to implement these changes.**

The shift in the benchmark, if accompanied by the adjustments that we propose, will have long-term benefits for the accuracy of HMDA reporting and in minimizing the impact of the additional HOEPA requirements on prime lending. At the same time, in the near and medium terms, the new rules will require systems changes that will impose a significant burden on the industry. In particular, the shift from monthly to weekly recalculations of the benchmarks will significantly increase the complexity of compliance and the corresponding risk of compliance errors.

In order to mitigate these burdens, the Board should allow sufficient time for the industry to come into compliance. Many lenders and vendors of HMDA software will be unable to make all necessary systems changes in time to begin capturing the new rate spreads in January 2009 as proposed, a mere four months away. Even if the software could be modified in time, it will be difficult to change manual procedures and conduct the extensive training that will be needed before January 1, 2009. Moreover, in order to be sure that all information fields needed for the rate-spread calculations are available for loans that may lock in 2009, some lenders would have to begin capturing that information immediately, even before the Board issues its final rules. This effort would be required even though the types of loans intended to be covered as “higher-priced mortgage loans” will not be originated in any quantity any time in the near future, and the problem is increasingly going to be the lack of credit availability, not the overextension of credit to marginal borrowers. In light of the considerable programming, training, and system testing required, we urge the Board to make the new data collection requirements effective, instead, on January 1, 2010.

Moreover, in the interest of consistency, the HOEPA rules should also apply starting at the beginning of the calendar year. Making the HOEPA rules effective during a calendar year imposes a significant compliance burden in itself and separate implementation dates for HOEPA and HMDA will make the 2009 HMDA data much more difficult to gather and may affect its quality. Separate systems would be necessary to identify the HMDA and HOEPA triggers. Moreover, changing HMDA data requirements during a year would make the data sets for that year internally inconsistent. Therefore, the HOEPA rules should also go into effect on January 1, 2010. The Board should also clarify that changes in the benchmark rates will be effective no more frequently than weekly, beginning on the first business day of the week following their publication by the Board. Even with these changes, the Board should be cognizant of the burden that these changes will create, as well as all of the other compliance challenges faced by the industry and at least for some period, regulatory compliance efforts should take appropriate account of compliance difficulties.

Finally, we note that the Proposal also raises a number of other technical issues, which are discussed in detail below.

Discussion

New Benchmark Indices

As noted, the Associations commend the Board for shifting the benchmark for rate-reporting from Treasury securities to rates derived from the PMMS. At the same time, it is essential that the Board establish separate benchmarks for markets, such as the jumbo loan market, in which the prime rate varies significantly from the conforming, conventional rate reported in the PMMS (see below). In the past, as the Board has noted in its discussions of HMDA “rate-spread” loan data, the proportion of subprime loans covered by the existing threshold has varied substantially from year to year depending on yield-curve changes and this change should help make progress toward diminishing the salience of this data issue. The “noise” in HMDA data created by the use of Treasury yields as the benchmark has created the misleading impression that lenders have changed their lending practices from year to year, when, in fact, changes in reported HMDA rate spreads have often been due to changes in the market.

Because the HMDA rate-spread threshold will now also be used as the trigger for coverage under the HOEPA “higher-cost” loan rules, it is critical that this anomaly be corrected. Therefore, we strongly support the proposed change in the benchmark index.

Adjustments for Different Mortgage Markets

Description of the Problem

Under the Proposal, the benchmark rate would be based on the applicable average prime offer rate (APOR) from the PMMS, plus 150 basis points for first-lien loans and 350 basis points for subordinate-lien loans. Because the PMMS is based on conforming loans with loan to value (LTV) ratios of 80% or less for conventional products, a benchmark based on the unadjusted APOR will not result in reporting an accurate rate spread over the average prime APR for prime loan types that are not included in the PMMS: jumbo non-conforming loans that will not be purchased by the GSEs; loans with LTVs above 80%, which typically have higher annual percentage rates (APR) due to mortgage insurance; and FHA loans. Many prime loans will be rate-reportable even though, as discussed below, the Board’s goal is to obtain rate-spread information and to provide special protections with respect to subprime loans and to exclude prime loans, and the number of loans falling into the “higher-priced” or subprime category will continue to be sensitive to changes in prime market risk and mortgage insurance premium rates. Even in the short time since the Board issued its proposal, market developments have caused the premium for loans that do not carry a government or government-sponsored enterprise (GSE) guarantee to increase. This is because, in part, the previously implicit government guarantee of GSE obligations has become more explicit, while there is still no functioning market for private securitizations.

For example, as shown in Attachment A, surveys of rates on jumbo loans indicate that the spread of the estimated APR on the average jumbo loan over the equivalent conventional rate has

exceeded 150 basis points over the estimated APR for the average comparable 30-year conforming loan every week, or almost every week, for the past six months, depending on which survey is used for the comparison. Moreover, these estimated APRs are based on reported points and fees and do not reflect settlement charges that are also included in the APR, so that the proportion of jumbo loans that would be covered by a 150-basis point spread over the PMMS is even higher than indicated in the surveys. In the current environment, very few jumbo loans are actually “subprime.” In fact, the opposite is the case; underwriting criteria for nonconforming loans have become stricter.

The HMDA rate-spread reporting requirement was designed to allow the Board and other interested parties to develop better data on the subprime mortgage market.⁶ Capturing data on large numbers of fully prime loans that are “rate-spread” or “higher priced” loans because of the market rate for the loan type rather than because they are subprime will undercut the Board’s reasons for instituting rate-spread reporting in the first place.

Moreover, because the same trigger will be used for coverage under the new rules for “higher-priced” loans under HOEPA, this is more than just a reporting issue. The “higher-priced” loan rules are aimed specifically at the subprime loan market, because the Board determined that there were special characteristics of that market that justified additional restrictions, requirements, and substantial civil liability even if the result was restricted availability of credit to borrowers who do not meet all of the requirements for a prime mortgage loan. Applying these special rules and additional liability to segments of the prime market such as jumbo loans or loans with loan-to-value ratios above 80% in which the higher APR reflects the cost of mortgage insurance is unwarranted. The Board determined that a certain category of loans is in need of greater protections under HOEPA; these loans are demonstrably outside of that category. While any combination of index and threshold will have some level of over-inclusion or under-inclusion, we believe that the degree of coverage of prime market products that would be caused by use of the benchmark without adjustment is too great and merits the minor adjustments to the Proposal that we recommend below.

The Board made it clear in issuing the HOEPA “higher-priced” rules that it defines subprime mortgage loans as those that “are made to borrowers who are perceived to have high credit risk.”⁷ It also noted that:

Consistent with this principle, the Board believes, as it stated in connection with the proposal, that the stricter regulations of § 226.35 should cover the subprime market and generally exclude the prime market.⁸

The Board’s adoption of a mortgage-based index is intended to reduce the impact of changes in market conditions over time on whether a loan is considered “subprime.” Similarly, the

⁶ See Board of Governors of the Federal Reserve System, Final Rule: Home Mortgage Disclosure, 67 Fed. Reg. 7222, 7229 (Feb. 15, 2002) (noting that the thresholds in the original rate-reporting rule were “intended to ensure, to the extent possible, that pricing data for higher cost loans are collected and disclosed, and at the same time to exclude prime loans from the requirement”).

⁷ 73 Fed. Reg. 44522, 44524 (July 30, 2008).

⁸ *Id.* at 44532.

adjustments that we propose are designed to reduce the impact on coverage of differences between market segments, and thereby bring coverage closer in line with the principle that the subprime market should be covered and the prime market should be excluded.

Moreover, we expect lenders to take a very cautious approach to making loans that exceed the “higher-priced” threshold due to the higher operational costs and civil liability risks associated with such loans. To the extent that lenders make these loans available, the market is likely to price them at higher rates that reflect the additional costs and legal risks, which translates into unnecessarily higher costs for consumers for whom the protections were not intended. Uncertainty relating to loan pricing and availability is likely to have a negative impact on real estate values for properties heavily affected by mis-designation as subprime.⁹

The Board indicated that it decided not to exclude jumbo loans from the higher-priced mortgage rules when it issued the HOEPA rule, assuming that the large current spreads over conforming loans would be a temporary phenomenon. Recent events have made predictions that the spread would soon narrow seem more and more problematic. In any event, the Board could address this uncertainty permanently by adopting our suggestion to adopt a separate benchmark rate so that the reported rate spread accurately reflects the amount by which the cost of a loan exceeds a valid prime rate for that loan category. The spreads between jumbo and conforming loans are likely to return to more normal historical levels once home prices and delinquency rates begin to improve, and if that occurs, the adjustments to the benchmark can narrow accordingly.

We are also concerned that the thresholds will undercut the potential effectiveness of the new Hope for Homeowners program that was added by the Housing and Economic Recovery Act of 2008 (HERA). Although the exact parameters of the program are not final yet, it appears that the annual mortgage insurance premium of 150 basis points under the program will by itself be sufficient to cause the APR on the loan to exceed the trigger rate in most cases. The mortgage insurance charges in the Hope for Homeowners program were mandated by Congress and do not reflect “subprime” loan pricing, deceptive marketing, or unfair loan terms – rather, these loans will be made under a government program that was created by Congress to allow borrowers to reduce their payments to an affordable level. It would be sensible from a policy perspective to keep these loans outside the ambit of “higher-priced mortgage loans” to facilitate borrower assistance under the program.

The Associations’ Proposal: Product-Specific Benchmarks

The Board is proposing to use the average prime offer rates (APOR) from the PMMS as the basis for its benchmarks. The benchmark would be the APOR for a given product type, plus 150 basis points for first-lien loans and 350 basis points for second-lien loans. If no APOR is available for a specific product type, the Board will estimate the rate based on the relative differences in yields of different Treasury products.

⁹ The impact on the marketplace is not just a theoretical concern. We note that Fannie Mae and Freddie Mac each recently announced that it would not purchase or securitize loans subject to New York’s new subprime law, because of concerns about their potential liability for origination issues over which they have no control. See Fannie Mae, Announcement 08-21, Purchase of New York “Subprime Home Loans” (Aug. 19, 2008) available at <https://www.efanniemae.com/sf/guides/ssg/annltrs/pdf/2008/0821.pdf>.

Adjustment for Jumbo Loans

While we support the Board's general approach, it does not account for the difference in prime market rates for different product types. We propose a similar method to adjust for the amounts by which the average prime rate for various market segments differs from the PMMS. The Board could conduct a periodic survey of the average amount by which the rate on "prime" loans in each category differs from the average prime, conforming loan rate, and add that spread to the general spread used for the reporting trigger and to report the rate on the loan. For example, as shown in Attachment A, the interest rate on the average prime jumbo loan currently exceeds the APOR for a loan that otherwise has the same characteristics (a 30-year fixed-rate loan with a loan-to-value ratio of 80% or less) by approximately 200 basis points. Therefore, the benchmark for such loans would be 200 basis points above the benchmark APOR for a prime conforming loan.

Adjustment for Private Mortgage Insurance Premiums

The Board should also provide a separate adjustment reflecting the average cost of "prime" borrower-paid mortgage insurance, based on the premium for a 95% loan-to-value ratio loan. This data could be gathered from the mortgage insurers – a separate survey of lenders would not be necessary. As shown by Attachment B, mortgage insurance increases the APR, although it does not reflect whether a loan is subprime but rather the amount of equity that the borrower has in the property. For example, as shown in Attachment B, in a typical purchase transaction by a prime borrower with a 95% LTV, the APR increased by 68 basis points.¹⁰ For larger loan sizes and for ARMs, the increase in the APR may be significantly greater. Borrower-paid mortgage insurance, however, is not reflected in the PMMS. While few, if any, high-cost loans under HOEPA carry mortgage insurance, many prime loans that would be reported under the proposed thresholds do carry insurance, and those premiums have been increasing in light of the softness in home prices.

Adjustment for FHA Mortgage Insurance Premiums

There should be a similar adjustment for the impact of FHA mortgage insurance premium on the APR, as well as for the impact of FHA premiums on loans originated under the Hope for Homeowners program. For the same reason that private mortgage insurance rates have been increasing, FHA rates have increased, and further increases and decreases can be anticipated once the moratorium on risk-based pricing expires on October 1, 2009. FHA recently announced an increase that will likely cause more FHA loans to exceed the trigger for coverage as "higher-priced mortgage loans."¹¹

¹⁰ As noted in Attachment II to this comment, the example is based upon a \$100,000, 30-year fixed-rate loan with rates and fees as shown in the May 15, 2008, PMMS and as reflected in Attachment I to the proposed rule.

¹¹ See Federal Housing Administration Single Family Mortgage Insurance: Announcement of Moratorium on Risk-Based Premiums, to be published in the *Federal Register* (available at http://portal.hud.gov/pls/portal/docs/PAGE/FHA_HOME/LENDERS/LENDER_DOCUMENTS/FR-S171-N-03.PDF).

Additional Benchmarks and Adjustments

In addition to the prime jumbo benchmark and special adjustments for both private and FHA mortgage insurance premiums, we recommend that the Board indicate in the final rule that it would be open to considering additional types of benchmark loans or additional adjustments to ensure that the threshold will accurately describe subprime loans without over-including prime loan products. For example, it may be appropriate to create a separate benchmark for construction-to-permanent loans, which generally carry a higher APR for the construction phase because the interest rate during that phase is tied to the commercial prime rate. Indeed, by definition, virtually all construction-to-permanent loans are prime loans that are made to highly-qualified borrowers who are able to carry the cost of both a construction loan and the mortgage or rent on their current residence. Flexibility should also be provided to adjust the benchmark as needed for government programs.

Timing of Publication and Effective Date of Benchmarks

While we strongly support reconciling the timing requirements for HMDA reporting with the rules for determining the higher-priced loan threshold under HOEPA, the Proposal is unclear on how often the benchmarks will be changed. The text of the proposed regulation states that the benchmarks will be updated “at least weekly,” while Attachment I to the Proposal indicates that they will be published on the Federal Financial Institutions Examination Council web site “by Thursday night.” Because loans could lock almost immediately after the rates are published, particularly in parts of the country where publication would occur during business hours, it will not be feasible to comply with the requirement to use “the most recently available” rate unless there is sufficient time to reflect changes in the benchmark in lenders’ systems.

In order to provide sufficient time, the effective date of the new benchmarks should be the first business day of the week following the publication of the benchmark (*i.e.*, the next Monday, or Tuesday, if Monday is not a business day for the reporting institution). Some lead time is necessary because, in contrast to the current HMDA rate-spread reporting rule, the new benchmark rates will affect not only reporting but also whether the HOEPA rules for higher-priced mortgage loans apply, which could affect the terms and cost of the transaction. Otherwise, lenders potentially would have only one business day, as opposed to the 15 calendar days or more for Section 226.32 loans,¹² to update the rate in their systems. Adapting to this accelerated schedule by the effective date of the HOEPA rule, October 1, 2009, will pose an operational challenge to many lenders, which is a further reason that we request a delay in the mandatory collection date for HMDA data and the effective date of the HOEPA rule until January 1, 2010. The Board should also clarify that benchmarks will change only once per week, even though the data underlying the benchmarks may be available more frequently than weekly. More frequent changes would unduly increase the regulatory burden and costs to consumers.

¹² The threshold rate for HOEPA high-cost loans is based on the comparable Treasury rate “as of the 15th day of the month immediately preceding the month in which the application for the extension of credit is received by the creditor. 12 C.F.R. § 226.32(a)(1)(i).

Effective Date

As noted, the Board has proposed that data collection under the revised rules begin on January 1, 2009, to accommodate the effective date of the HOEPA amendments, October 1, 2009. Considering that this is a mere four months away, this deadline will pose an unnecessary, undue, and very costly burden on reporting lenders. While it is true that the actual HMDA report will not be due until March 1, 2010, all of the fields of information needed to calculate the spread would have to be captured at the time of application if the loan might reach final disposition in 2009. Effectively, this means that lenders would have to establish systems to capture these fields for applications that they are taking now, even before the revised rules are promulgated. The new rules will require changes in systems, procedures, and training that will be nearly as extensive as those that were needed to institute rate-reporting in the first place. They will require adjustments in the benchmark rate to be made weekly rather than monthly and will require institutions to track many more indices than they do under the current rules. In terms of compliance cost and complexity, we note that the intricacy of compliance is multiplied, and the risks of compliance lapses are intensified, when there is a regulatory variable that changes on a weekly basis. Although these risks may be inherent to ensuring that the thresholds are more accurate in terms of market movements, the compliance burdens it provokes are very real and a concern to lenders of all sizes. For this reason we also suggest that at least initially compliance officials should be mindful of these difficulties and should take them into account in avoiding any sanctions.

Lenders have various arrangements to capture rate-spread information under the current rules. In some instances, the information used to calculate the spread (lock date, term in years, lien position, and APR) may be contained in an origination system that calculates the spread – under the current rules – and passes the spread information to another system. It would be very costly to record the information under the current system and then later recalculate the spread under the new rules. Also, existing systems used for HMDA reporting may not capture information such as whether a loan is an adjustable-rate mortgage that would be needed to report correctly under the new rules. Moreover, many lenders have multiple (or even numerous) systems for originations through their different channels, including legacy systems.

We also note that mortgage lenders currently face many other systems challenges based on legislative and regulatory changes. These include implementing systems changes to conform operations to (i) Federal Housing Administration changes to implement the moratorium on risk-based pricing, (ii) efforts to gear up for the Hope For Homeowners program, (iii) the new Regulation Z changes affecting both origination and servicing, (iv) the new amendments to TILA enacted by Congress in the Mortgage Disclosure Improvement Act that was enacted as part of HERA, (v) loan originator licensing and registration requirements, and (vi) numerous changes to state laws, especially changes to default and foreclosure rules. In addition to these known changes, HUD has submitted to the Office of Management and Budget for review a final Real Estate Settlement Procedures Act rule that will also require substantial systems modifications. All of these changes will result in unparalleled implementation and compliance costs at a time when limited resources available to the mortgage industry.

The proposed deadline of January 1, 2009, to begin recording rate spreads under the new system would require institutions to divert resources from these other important projects and implement

the HMDA-reporting changes on a “crash” basis. To avoid such a misallocation of resources, we strongly urge the Board to make the new data collection requirements effective, instead, on January 1, 2010, following the effective date of the HOEPA rules.

In addition, making the HOEPA rules effective during calendar year 2009, while the HMDA rules would go into effect at the beginning of a calendar year (either 2009 or, as we have suggested, 2010), would necessitate additional costs and make it even more complicated to implement the changes, reducing the benefits of moving to the same rate-spread calculation method for HMDA and HOEPA. As discussed in detail below, if the effective date for HMDA and HOEPA are not aligned, then complex transition rules would be necessary. Therefore, the Board should also make the HOEPA amendments effective on January 1, 2010.

Transition Rules

The Board has adopted an October 1, 2009, effective date for the HOEPA rules and proposes a January 1, 2009, effective date for data collection under the new HMDA rate-spread rules. Because of the system disparities and consequent complexity of maintaining differing systems for calculating the rate spread, the effective date for both HOEPA coverage and HMDA data-collection should be shifted to January 1, 2010. As discussed above, the shift to weekly reporting will create a significant compliance challenge, especially when combined with the many other new compliance challenges that the industry is facing at the same time.

If the Board does not delay the effective date of either HMDA data-collection or the new HOEPA requirements, reporting will be extremely complicated and burdensome and the quality of the data may be compromised as a result. Because of these difficulties, if the Board does not delay either effective date, it should clarify that, during calendar year 2009, an institution will be deemed to be in compliance with any requirement to update the Loan Application Register quarterly if it has timely recorded all the information other than the rate spread and has retained sufficient information so as to be able to generate and report a rate spread before the annual filing deadline. Failing to provide such relief would as much as ensure that any institution subject to quarterly reporting requirements that continues to make mortgage loans will be risking non-compliance.

If the Board grants our request to set a uniform compliance date of January 1, 2010, a simple rule will still be needed to account for loans in which the application is taken, and the rate is locked, in 2009, but the loan does not close until on or after January 1, 2010. We suggest that the Board take the same approach that it took when it instituted reporting of the rate spread and other new fields in 2004, and give lenders the option of reporting loans that lock in 2009 but close in 2010 under either the old or the new method of calculating the rate spread.¹³

Finally, if the Board delays HMDA data-collection under the new rules until January 1, 2010, but retains the effective date of October 1, 2009, for the new HOEPA rules, then lenders will need to maintain different systems for identifying HOEPA loans on the one hand, and HMDA-reportable loans on the other, unnecessarily increasing costs and confusion. To avoid this problem, the

¹³ See 68 Fed. Reg. 31589 (May 28, 2003), *codified in* the Official Staff Commentary to Regulation C, 12 C.F.R. pt. 203 supp. I, § 203.4(a)-4.v.

Board should adopt a transition rule providing that either the old or new HMDA spread calculation may be used for (1) applications received before October 1, 2009, that are originated in 2010 and are reported on the 2010 LAR, and (2) applications received on or after October 1, 2009, that are originated in 2009 and are reported on the 2009 LAR.

Our proposed transition schedule is illustrated in the following table:

Application Date	Rate Lock Date to Consumer	Origination Date	Subject to HPML Rule?	Old or New Spread?
Before Oct. 2009	Before Oct 2009	2009	No	Old
Before Oct 2009	Oct 2009 –Dec 2009	2009	No	Old
Before Oct.2009	Before Oct 2009	2010	No	Old or New
Before Oct.2009	Oct 2009 – Dec 2009	2010	No	Old or New
Before Oct.2009	2010	2010	No	Old or New
Oct 2009 – Dec 2009	Oct 2009 – Dec 2009	Oct 2009 – Dec 2009	Yes	Old or New
Oct 2009 – Dec 2009	Oct 2009 – Dec 2009	2010	Yes	New
Oct 2009 – Dec 2009	2010	2010	Yes	New
2010	2010	2010	Yes	New

This proposal makes the following assumptions:

- The Higher-Priced Mortgage Loan (HPML) rules under HOEPA will be effective with applications received by a table-funded broker or creditor on or after October 1, 2009.
- Except as modified by transition rules, the old HMDA rate-spread calculation will be used for the 2009 LAR and the new HMDA rate-spread calculation will be used for the 2010 LAR.
- In applying the transition rule, the application dated reported on the LAR will be used to determine the date the application is received. Consistent with the Regulation C Commentary,¹⁴ when an application is forwarded by a broker, the reporting institution may report the date the application was received by the broker, the date the application was received by the reporting institution, or the date shown on the application.

In light of the normal time between application and loan closing, the proposed transition rule would affect relatively few loans – the overwhelming majority of loans reported on the 2009 LAR would use the old HMDA rate-spread calculation and the overwhelming majority of loans reported on the 2010 LAR would use the new HMDA rate-spread calculation. Because consumers would be protected by the HPML rules effective with applications received on or after October 1, 2009, the transition rule would lessen reporting burdens without harming consumers.

In the case of an application to a table-funded broker where the loan is reported by a funding lender that conducts a pre-closing review, the transition rule would provide that:

¹⁴ See 12 C.F.R. pt. 203 supp. I § 203.4(a)(1)-2.

- The determination of whether the loan is subject to the HPML rule depends upon the date of the application to the table-funded broker, not the date the application is received by the funding lender.
- The funding lender has the choices noted above for the reporting of the application date on its LAR.
- To determine the index value for HPML purposes, the date that the rate is set by the broker to consumer is used. To determine the index value for HMDA rate-spread purposes, the date the rate is set by the funding lender to the broker is used.

Finally, it should be noted that, as a result of these variations, the fact that a rate spread is or is not reported will not indicate whether the loan is a HPML.

Technical Issues Raised by the Proposal

The proposal to use the APOR as the basis for coverage and for computing the rate spread raises a number of technical issues:

- **Determination of comparable transaction period.** The final rule should clarify a number of issues related to identifying the comparable transaction period:
 - **Fixed rate loans.** The regulation should confirm that, for a fixed rate loan, the comparable transaction is determined using the term of the loan in years.
 - **Variable rate loans.** The rules for variable rate loans should specify that the comparable transaction is determined using only the period to the first adjustment (rather than the period between adjustments thereafter).
 - **Step-rate and balloon loans.** The Proposal does not explicitly address step-rate or balloon loans. We suggest that step-rate loans be treated in the same way as fixed-rate loans, so that the comparable transaction would be determined using the term of the loan in years. For balloon loans, we suggest that if the loan has a fixed rate before the balloon comes due it should be treated as a fixed-rate loan, unless it is a renewable balloon loan with conditions within the borrower's control as described in the Official Staff Commentary to Regulation Z,¹⁵ in which case it should be treated as a variable-rate loan with a first adjustment at the time the balloon comes due.
- **Method used to convert PMMS to APRs.** The Proposal notes that the 5/1 ARM product described by the PMMS is adjusted annually after the initial 5-year period using the 1-year Treasury rate plus a margin. In computing the fully-indexed rate that will be used in the APR calculation for this product, however, the Proposal adds the margin that was reported in the PMMS for the 5/1 product to the 5-year Treasury rate rather than to the 1-year Treasury rate. Because the 5-year Treasury rate is higher than the 1-year Treasury actually used by lenders in resetting the rate on the loan, this approach appears to increase the fully indexed rate, the

¹⁵ See 12 C.F.R. pt. 226 supp. I, § 226.17(c)(1)-11.

APR and the threshold significantly. The APR with the 5-year Treasury was 5.82% while the APR with the 1-year Treasury would be 5.16%. The calculation of the fully-indexed rate for the 2, 3, 7 and 10-year variable rate loans for which an APOR is calculated uses the 2, 3, 7 and 10-year Treasury rates respectively, so all seem to be similarly increased. We understand that the Board plans to clarify whether it intends for the Treasury rate corresponding to the initial term to be used to compute the fully-indexed rate.

- **Assignment rules if no matching APOR.** Currently under Regulation C, if there is no Treasury security yield that exactly matches the maturity of a loan, the yield used is the yield that is closest to the loan’s maturity, and if the loan’s maturity is exactly halfway between security maturities, the lower Treasury Security yield is used. This method follows the method used for HOEPA loans as described in the Regulation Z Commentary.¹⁶ The discussion in Attachment I to the Proposal of “assignment rules” appears to indicate that if the term of the loan (for a fixed-rate loan) or the initial adjustment period (for a variable-rate loan) does not have a matching APOR, the next longest APOR should be used. The final regulation should explicitly state these assignment rules.
- **Use of surveys other than PMMS.** The Proposal reserves the right for the Board to conduct its own surveys if it becomes appropriate or necessary and that the benchmark published in these circumstances may consider other loan pricing terms including indices, margins, initial and fixed rate periods for variable rate transactions and the consumer’s credit history, loan-to-value ratio, owner-occupant status and loan purpose. While we support this flexibility, we note that reporting institutions will need considerable lead time to program their HMDA reporting systems if new fields of information must be used to determine the benchmark for a comparable transaction. Unless the Board intends to give reporting institutions at least 9 months’ lead time before a new field of information must be used and require the new field only as of January 1 of the next calendar year, we recommend that the final rule identify any additional fields of information that potentially may be used to determine the comparable transaction with the specificity needed to complete programming now.
- **Changes in method of identifying comparable transaction.** The Proposal indicates that the table that sets forth the benchmarks will “indicate . . . how to identify the comparable transaction.” This implies that, if the table is updated, the method for identifying the comparable transaction could change. If the method changes, reporting institutions will need sufficient lead time to make the necessary programming changes.
- **HOEPA flag.** The regulation should clarify that only the “high-cost” loans subject to Section 226.32 of Regulation Z are to be coded as high-cost loans on the HMDA Loan Application Register.
- **Other products.** The Proposal does not address how to apply the rate-spread rules to a number of other products. We request that the Board address these issues—and other issues related to product types that are not addressed in the Proposal—in the Commentary or in other guidance available before the effective date of the changes in the regulation. By way of example, the Proposal does not address interest-only ARMs, where the monthly payment for

¹⁶ See 12 C.F.R. pt. 226 supp. I, § 226.32(a)(1)(i)-4.

the initial fixed rate period is interest-only, followed by a fully-amortizing ARM over the remaining term. One of many variations of this product involves a loan with a term of 40 years that is fixed-rate, interest only for the first 15 years, at which time there is a one-time interest rate adjustment, with the loan then fully amortizing for the remaining 25 years. Given that market and regulatory changes have eliminated or reduced the availability of many non-traditional products that previously were widely available, the Board should consider how to provide authoritative guidance for lenders that implement new affordability products.

- **Interpolation method.** We also recommend that the Board consider revising the method for calculating through interpolation the implied APOR values for instruments with maturities for which no PMMS data is available. Instead of using an absolute mortgage credit spread (the difference between the APR on a 1-year instrument and the 1-year PMMS), the Board should use a relative mortgage credit spread (the 1-year APR divided by the 1-year PMMS). Such an approach would be consistent with the widely-held view that credit risk spreads depend, in part, on the level of interest rates. For example, the credit-risk spread at a given risk premium is higher when the prevailing level of rates is 3.0%, rather than 10%.

Thus, for example, using the May 15, 2008, data contained in the Board's example (Attachment I of the Proposal), rather than calculating the one year credit spread in absolute terms as 5.18% (the rate given by the survey for one-year ARMs) minus 2.07% (the average one year rate) to obtain an absolute risk spread of 3.11%, the risk premium would be calculated in relative terms, as 5.18% divided by 2.07%, or 2.50. Using the same approach, the five-year relative spread would be 1.78. Continuing with the same weighting approach proposed by the Board, the weighted average starting rate for a two-year instrument would then be 5.64%, rather than 5.54%, and the implied APOR (after adjusting for points using the same method as proposed by the Board) would be 5.02%, rather 4.97%.

While this is not a large adjustment, it would further improve the accuracy of the benchmarks used to report rate spreads.

- **Provision of complete benchmark data.** To accommodate institutions that will be processing rate changes manually, the Board should provide all applicable benchmarks for each week. If the Board adopts our recommendation to make adjustments for market segments in which the prime rate is different, the Board's release should show all possible combinations of benchmark rates for each loan term, such as "conventional loan without mortgage insurance," "conventional loan with mortgage insurance," "jumbo loan without mortgage insurance," etc.
- **Determination of date rate is set.** Lenders use different methods to lock their rates, and operational burdens will be substantially lessened if the final rule permits some flexibility. For example, many lenders set a base rate that varies with market conditions, and then apply a "rate adjuster" that varies based on characteristics of the loan such as the loan-to-value ratio. As a result, a rate may be locked as of a specific date, but the rate may later change when updated information (such as an appraised value higher or lower than initially estimated) changes the rate adjusters that apply to the loan. In these cases the lender will often keep the base rate the same as the base rate on the original rate lock date, but increase

or reduce the adjuster to reflect the updated information. In effect, the lender locks the base rate and the amount of the adjusters that may apply, but does not determine which adjusters apply until the characteristics of the loan are determined.

If a rate lock agreement has been executed indicating that the base rate and the applicable adjusters as of the original lock date will be used, lenders should have the option of not changing the date for determining the benchmark, because the benchmark reflects market conditions when the base rate was set. On the other hand, other lenders do not use “base-rate locks” and if the rate changes after it is initially locked they would want to report the most recent date that the interest rate changes. We recommend a clarification that lenders have the option of using either the original date that a base rate was locked, or the date of the last rate lock before closing, to determine the applicable benchmark rate, so long as the lender’s approach is generally consistent. Permitting minor variations in the reporting of the date the rate is set would be similar to the current rules for reporting the “application date,” where the lender may choose from a number of options so long as lender’s practices are “generally consistent.”¹⁷

* * *

With the minor changes that we have recommended, we believe the Board could implement the changes to the Regulation C threshold for reporting “rate-spread” loans and set the threshold for the new HPML loans with a greatly reduced harm to the prime mortgage market and burden to reporting financial institutions. We appreciate the opportunity to present our views.

American Bankers Association
American Financial Services Association
Consumer Bankers Association
Consumer Mortgage Coalition
Mortgage Bankers Association

¹⁷ See Official Staff Commentary to Regulation C, 12 C.F.R. pt. 203 § 203.4(a)(1)-1.

Attachment A: Impact of Proposed Rate Spread on Jumbo Loans

One of the key problems with using a trigger of 150 basis points over the Freddie Mac rate in the current environment is the impact on jumbo loans. While 30-year fixed rate jumbo loans historically carried spreads of from 1/8th to 3/8ths over GSE conforming loans presenting comparable risks, those spreads have widened considerably since the collapse of the private-label market in mid-2007 and now are approximately 200 basis points. Since a wholesale triggering of jumbo loans would even further restrict credit in this market, it is important to understand the potential number of prime loans that would be reportable under the Proposal, and, therefore, subject to the requirements for “higher-priced mortgage loans” under HOEPA .

Various sources of information of jumbo loan rates exist. One complicating factor, however, is that recent actions by Congress have changed the definitions of what constitutes a jumbo loan. The Housing and Economic Recovery Act provided for increases in the maximum loan amounts of loans eligible for purchase by Fannie Mae and Freddie Mac, or insured by FHA (http://www.ofheo.gov/media/hpi/AREA_LIST_5_2008.pdf).

These maximum amounts differ from area to area based on the area’s median home price up a maximum of \$729,750 in the highest-priced areas. While the maximum loan limits for the highest-priced areas will decrease to \$625,500 after January 1, 2009, the problem of what will or will not be a jumbo loan for pricing purposes based on geographical location will continue. Therefore, it is important to distinguish between those jumbo loans that are eligible for GSE purchase and those that are not. Most of the sources of jumbo loan rates do not make this distinction.

One source that has recently started to make this distinction is the publication *Inside Mortgage Finance* (IMF). IMF publishes the Freddie Mac survey rate for fixed-rate 30-year conforming loans, its own survey rate for 30-year conforming loans, the rate for jumbo loans, and, since mid-April 2008, the rate for jumbo loans eligible for GSE purchase. In addition to the contract rates, IMF publishes the points associated with the loan so it is possible to do APR comparisons between the loans. The Freddie Mac and IMF rates from March 14, 2008 through August 15, 2008 are shown below, together with the points:

	Freddie Mac 30-yr FRM		IMF 30-yr FRM Conforming		IMF 30-yr Jumbo Agency Eligible		IMF 30-yr Jumbo Not Agency Eligible	
	Rate	Points	Rate	Points	Rate	Points	Rate	Points
3/14/2008	6.13	0.50	6.17	1.44			7.71	2.50
3/21/2008	5.87	0.50	5.54	1.44			7.63	1.50
3/28/2008	5.85	0.40	5.67	1.50			7.67	2.30
4/4/2008	5.88	0.50	5.83	1.38			7.50	2.56
4/11/2008	5.88	0.40	5.63	1.56	6.13	1.50	7.04	2.69
4/18/2008	5.88	0.40	5.96	1.38	6.44	1.56	7.38	2.75
4/25/2008	6.03	0.30	5.83	1.50	6.25	1.50	7.33	2.81
5/2/2008	6.06	0.50	5.94	1.25	6.83	1.79	7.38	2.81
5/9/2008	6.05	0.30	5.94	1.29	6.75	1.83	7.38	2.63
5/16/2008	6.01	0.60	6.03	1.29	6.63	1.63	7.38	2.69
5/23/2008	5.98	0.50	5.84	1.29	5.81	1.38	7.50	2.67
5/30/2008	6.08	0.60	6.06	1.38	6.00	1.44	7.78	2.13
6/6/2008	6.09	0.60	6.03	1.25	6.71	1.92	7.50	2.81
6/13/2008	6.32	0.70	6.22	1.38	6.88	2.04	7.63	3.31
6/20/2008	6.42	0.70	6.44	1.46	6.38	1.44	7.79	3.25
6/27/2008	6.45	0.60	6.44	1.38	6.38	1.44	7.75	3.19
7/4/2008	6.35	0.60	6.00	1.88	6.13	1.88	7.58	2.13
7/11/2008	6.37	0.60	6.16	1.50	6.17	1.50	7.69	3.00
7/18/2008	6.28	0.60	6.12	1.50	6.17	1.56	7.81	2.81
7/25/2008	6.63	0.60	6.50	1.40	6.54	1.20	8.20	3.40
8/1/2008	6.52	0.70	6.35	1.38	6.33	1.44	8.18	3.13
8/8/2008	6.52	0.70	6.48	1.38	6.46	1.43	8.30	3.25
8/15/2008	6.52	0.70	6.41	0.85	6.38	1.25	8.31	1.44

The APRs calculated based on the above rate and fee calculations are given below:

	Freddie Mac 30-yr FRM	IMF 30-yr FRM Conforming	IMF 30-yr Jumbo Agency Eligible	IMF 30-yr Jumbo Not Agency Eligible
	APR	APR	APR	APR
3/14/2008	6.18	6.31		7.97
3/21/2008	5.92	5.67		7.79
3/28/2008	5.89	5.81		7.91
4/4/2008	5.93	5.96		7.77
4/11/2008	5.92	5.77	6.27	7.31
4/18/2008	5.92	6.09	6.59	7.67
4/25/2008	6.06	5.97	6.39	7.62
5/2/2008	6.11	6.06	7.01	7.67
5/9/2008	6.08	6.06	6.93	7.65
5/16/2008	6.07	6.15	6.79	7.66
5/23/2008	6.03	5.96	5.94	7.78
5/30/2008	6.14	6.19	6.14	8.01
6/6/2008	6.15	6.15	6.90	7.79
6/13/2008	6.39	6.35	7.08	7.98
6/20/2008	6.49	6.58	6.52	8.14
6/27/2008	6.51	6.57	6.51	8.09
7/4/2008	6.41	6.18	6.31	7.80
7/11/2008	6.43	6.30	6.31	8.01
7/18/2008	6.34	6.26	6.32	8.11
7/25/2008	6.69	6.64	6.66	8.57
8/1/2008	6.59	6.48	6.47	8.52
8/8/2008	6.59	6.61	6.60	8.66
8/15/2008	6.59	6.49	6.50	8.47

Based on these APRs, the spreads are given below in basis points.

APR Spreads (in basis points)				
	IMF 30 yr conforming – Freddie Mac 30yr FRM	IMF GSE eligible jumbo – IMF 30 yr conforming	IMF jumbo – IMF 30 yr conforming	IMF jumbo – Freddie Mac 30 yr FRM
3/14/2008	13		167	180
3/21/2008	-24		211	187
3/28/2008	-8		210	202
4/4/2008	3		181	184
4/11/2008	-14	49	154	140
4/18/2008	17	50	158	175
4/25/2008	-8	42	165	156
5/2/2008	-5	95	161	156
5/9/2008	-2	87	159	157
5/16/2008	9	64	151	159
5/23/2008	-7	-2	182	175
5/30/2008	5	-5	181	187
6/6/2008	0	75	165	165
6/13/2008	-4	73	163	159
6/20/2008	9	-6	156	165
6/27/2008	7	-6	152	158
7/4/2008	-23	13	162	139
7/11/2008	-12	1	170	158
7/18/2008	-7	6	185	177
7/25/2008	-5	2	194	188
8/1/2008	-10	-1	204	193
8/8/2008	3	-2	204	207
8/15/2008	-10	1	197	188

The table on the APR spreads shows that the spreads on jumbo loans not eligible for GSE purchase have exceeded 150 basis points over comparable 30-year conforming loans every week for the past six months. Even when compared with the APRs calculated on the Freddie Mac survey of 30-year conforming rates, spreads have exceeded 150 basis points every week but two.

While there are no doubt shortcomings in the IMF data, just as there are in any survey of this type, the data are important because both conforming and nonconforming data come from the same companies. Companies that report conforming 30-year fixed-rate mortgages to IMF also are, by and large, the same firms that report jumbo rates to IMF. The result is that the spreads more accurately reflect what is going on in the market than surveys that combine many different reporters with different rate/fee combinations, even if the level of the rates differs from other surveys. Indeed, for the 30-year fixed-rate mortgages, the IMF APRs are only slightly lower than those calculated based on the Freddie Mac survey.

One other issue with the data is that surveys of jumbo rates without reference to points can be particularly misleading in this market. The normal convexity characteristics of large-balance loans are exacerbated by the huge pre-payment incentives impounded in recent spreads, that is, these loans are likely to pre-pay very quickly as spreads begin to return to normal levels regardless of what happens to underlying interest rates. Since charging higher contract rates would only make the potential prepayment incentives worse from the lenders' or investors' points of view, lenders have turned to larger amounts of points to achieve the required return on the mortgages. Therefore, reported contract rates on jumbo loans are far below what an equivalent par (zero point) rate would be, thus calling into question any jumbo rate survey that does not include points.

It should also be noted that the spread between jumbo loans eligible for GSE purchase and on-jumbo GSE loans has narrowed considerably. The important issue here is that the difference between a spread of 6 basis points for the week of July 18 and a spread of 185 basis points relates to whether the loan was eligible for GSE purchase, not to loan characteristics. A \$600,000 loan made in Arlington, Virginia, where it is GSE-eligible, would not be covered whereas that exact same loan with the same borrower and collateral risk-characteristics made in Richmond, Virginia, where it is not GSE-eligible, would be covered. First, this proposed rule makes it less likely that the loan in Richmond would be made. Second, it is not clear what public purpose is served in creating a checkerboard of triggered loans that will increase lender liability based solely on the vagaries of home-price calculations.

Attachment B: Impact of Proposed Rate Spread on Loans with Mortgage Insurance

The primary difficulty facing the mortgage market today is the large number of homes for sale. In order to clear this backlog, it is imperative that credit to prime borrowers who are able to make reasonable down payments not be impaired. Mortgage insurance is generally required in prime purchase transactions with LTVs above 80%, and the APR on such prime transactions is significantly higher. In the example below, a purchase transaction by a prime borrower with a 95% LTV, the APR increased by 68 basis points (.68%). The example is based upon a \$100,000, 30 year fixed rate loan with rates and fees as shown in the May 15, 2008, PMMS and as reflected in Attachment I to the proposed rule. For larger loan sizes and ARMs, the increase in the APR may be significantly greater.

Typical Borrower-Paid Monthly MI Premiums

	LTV / MI Cov.	> 25 Yr Fixed Rate (including 5/1, 7/1, 10/1 ARMs)		≤ 25 Yr Fixed Rate		3 Yr ARMs		1 Mo, 6 Mo, & 1 Yr. ARMs	
		700+	680-699	700+	680-699	700+	680-699	700+	680-699
Base Rates	97 / 35	.98	1.10	.87	.99	1.14	1.28	1.20	1.39
	95 / 30	.94		.73 (25% cov)		1.04		1.08	
	90 / 25	.62		.33 (12% cov)		.73		.78	
	85 / 12	.38		.23 (6% cov)		.39		.44	
Adjustors	Rate/Term Refi	+ .05		+ .05		+ .05		+ .05	
	Cash Out Refi	+ .10		+ .10		+ .10		+ .10	
	Loan Amt. > \$417,000	+ .25		+ .25		+ .25		+ .25	

Notes:

1. After 10 years, the MI Renewal Rate drops to .20 plus adjustors, if any.
2. MI is generally not available for FICOs below 620. For LTVs of 95% or less, MI premiums are the same for all FICOs above 620.
3. Under the Homeowners Protection Act, MI will terminate when the LTV reaches 78% or the midpoint of the amortization period.

Example Based on Primary Residential Purchase Transaction

95% LTV, 30 Year Fixed Rate Loan

6.01% Fixed Rate and .6 Points & Fees (Per May 15, 2008 PMMS)

Loan Amount = \$100,000

MI Rate for first 10 years = .94

\$100,000 x .0094 = \$940 per year / 12 months = \$78.34 per month

MI Renewal Rate after 10 years = 0.20

\$100,000 x .0020 = \$200 per year /12 months = \$16.67 per month

APR Calculation based on 6.01% interest rate and Amount Financed of \$99,400.

(Loan amortizes to 78% of original FMV of \$105,263 after 129 payments, at which point Mortgage Insurance is subject to cancellation and is not reflected in the APR)

120 payments of $\$600.19 + \$78.34 = \$678.53$

9 payments of $\$600.19 + \$16.67 = \$616.86$

231 payments of 600.19

APR – 6.75% (compared to 6.07% without Mortgage Insurance per Attachment I of the Proposed Rule)