April 11, 2007 via facsimile

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In re: Proposed Statement on Subprime Mortgage Lending (FR Doc. E7–4102)

The American Credit Union Mortgage Association (ACUMA) would like to contribute the following comments regarding the Proposed Statement on Subprime Mortgage Lending:

ACUMA shares the concerns of the Agencies that subprime mortgage borrowers may not fully understand the risks and consequences of obtaining certain adjustable-rate mortgage (ARM) products, but ACUMA also feels that any efforts in this arena should be expanded beyond just subprime mortgage borrowers.

Credit Unions remain to this day a leader in serving low- and moderate-income borrowers as evidenced by the 2005 Home Mortgage Disclosure Act data[1], which shows that Credit Union approval rates, to low- and moderate-income borrowers, is 70.8% compared to others which have a 46.3% approval rate. Low- and moderate-income borrowers tend to have their credit adversely affected by various life events more so than higher income borrowers and Credit Unions have been serving these consumers for almost three-quarters of a century without the issues being faced today. Credit Unions have a well-deserved reputation for being pro-consumer, pro-disclosure and for not placing borrowers in loan products that may have a negative impact on their future ability to make payments.

The recent Interagency Guidance on Non-traditional Mortgage Lending, that prohibits qualifying borrowers based on introductory or start-rates, proscribes that the underwriting analysis must demonstrate that a borrower is able to afford the new debt at a fully-indexed rate. This will have a future positive effect on the American Consumer being able to afford the loan at the time of application and well into the future. Unfortunately the current rate of default and foreclosure throughout the Country is a result of consumers not being able to afford the payment shock attributed to Non-traditional Mortgage products, to include various ARM products, which unscrupulous lenders have provided to borrowers, using unrealistic “start” rates to calculate unrealistic qualifying debt ratio to those who did not have the level of income necessary to absorb the changes in future payments. Many states are implementing this guidance verbatim as law, and other states are using this as a framework for proposed legislation that will hopefully reduce the number of foreclosures in the future.

[1]Credit Union National Association calculations based on Federal Reserve 2005 HMDA data.

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The American Consumer is often deceived by unscrupulous mortgage advertisements and lenders that do not have the borrower's best interest in mind. ACUMA would like to see more stringent advertising laws and regulations as it relates to mortgage rates and or programs.

Lenders know that a particular rate they are advertising requires a pre-payment penalty, whether there is a likelihood that deferred interest will ensue, and whether the borrower will face payment shock in the future with a particular rate and/or program. It is unfortunate that our legislators and regulators feel strongly about advertising restrictions for things such as tobacco related products, but do not take the same level of concern for the advertising of mortgage products that can have drastic impact on the financial security and quality of life of the American Consumer.

Presently, lenders must comply with rate advertisement requirements that dictate that the annual percentage rate (APR) *must be in the same size type and font as the rate*. Imagine if lenders also had to state whether a particular rate/program *has a pre-payment penalty, the potential for deferred interest and/or the potential for volatile payment changes in the same size type and font as the rate/APR*. We think it would be a great benefit for the American Consumer to have every opportunity to know this information even before applying. By placing restrictions on mortgage print and voice advertising, lenders would be required to indicate if a loan rate and/or product offering has the type of risks analogous to tobacco products or certain pharmaceutical products. These type of changes could go a long way in educating the American Consumer to steer away from harmful mortgage loan programs.

ACUMA encourages legislators and regulators to address the items discussed above in an effort to assist the American Consumer's ability to better understand the risks and consequences of obtaining certain adjustable-rate mortgage (ARM) products. ACUMA salutes the Agencies' directive in this area and hopes that further work can be done to assist American Consumers from choosing mortgage loan products that are not in their best interest.

The following are specific comments, as requested, concerning the Proposed Statement on Subprime Mortgage Lending:

1) The proposed qualification standards are likely to result in fewer borrowers qualifying for the type of subprime loan addressed in this statement, with no guarantee that such borrowers will qualify for alternative loans in the same amount. *Do such loans always present inappropriate risks to lender or borrowers that should be discouraged, or alternatively, when and under what circumstances are they appropriate?*

Lenders must take into account proper risk management best practices when creating loan programs. The non-traditional ARM programs, that many American Consumers have, were better designed for more experienced and financially astute borrowers. Unfortunately some lenders made these programs available to third-party origination distribution channels, without proper underwriting guidelines to include verification of income or employment, which has allowed unscrupulous lenders to put borrowers at risk by purchasing homes that they could not afford or into high loan-to-value debt-consolidation refinances which have jeopardized the viability of the borrower being able to keep their home when payments increased in the future.

Proper disclosure (to include more stringent advertising laws and regulations) of the imminent risk with any particular loan program and the Interagency Guidance on Non-traditional Mortgage Lending will go a long way to ensure future borrowers do not face the situation that many American Consumers now find themselves in.

Lenders do not make money when borrowers default, and open market pressures should dictate proper risk management attributes that will lead to a correction with the assistance of the Regulatory agencies. ACUMA would encourage Lenders and any agency that is charged with oversight of the Government Services Enterprises (GSEs: FNMA, FHLMC, FHLB, etc.), to create sound programs that will allow American Consumers to refinance out of loans that were not in the best interests of the borrowers and allow them an opportunity to keep the home they and their families reside. This might also require the use of alternative qualifying standards for certain ethnic based consumers who may not historically use traditional credit or have unverifiable income streams.

2) *Will the proposed statement unduly restrict the ability of existing subprime borrowers to refinance their loans and avoid payment shock*? The agencies also are specifically interested in the availability of mortgage products that would not present the risk of payment shock.

It is quite possible that some existing subprime borrowers will not be able to refinance their loans. If they are assessed a prepayment penalty, have a larger than original outstanding loan balance due to deferred interest/negative amortization, or income limitations that restrict them from qualifying for a new loan instrument, there could be difficulty meeting the new qualifying standards.

The GSEs could utilize their existing expanded approvals to meet much of this demand, but their guidelines will also need to be amended to achieve the flexibility needed to allow for loan-to-values that may need to exceed 100% of value in some cases to ensure American Consumers can keep their homes and remain contributing members of their communities.

3) *Should the principles of this proposed statement be applied beyond the subprime ARM market?*

Yes; these principles would benefit the health of the overall industry and hopefully restore the confidence that lenders do have the interests of the American Consumer in mind.

See also comments supra regarding enhanced disclosure and advertising regulations.

4) We seek comment on the practice of institutions that limit prepayment penalties to the initial fixed rate period. Additionally, we seek comment on how this practice, if adopted, would assist consumers and impact institutions, by providing borrowers with a timely opportunity to determine appropriate actions related to their mortgages. We also seek comment on whether an institution's limiting of the expiration of prepayment penalties such that they occur within the final 90 days of the fixed rate period is a practice that would help meet borrower needs.

Credit Unions are prohibited from providing mortgage loans with pre-payment penalties.

Pre-payment penalties were originally created to ensure lenders would receive a market interest rate for a minimum period of time rather than to charge American Consumers a higher interest rate. Unfortunately, the use of third-party origination distribution channels has led to prepayment penalties being used by lenders to not only ensure that they receive a market interest rate for a given period, but now also to ensure that the lender recoups any yield spread premium (YSP) (American Consumers receive a higher than market rate) paid to the third party origination distribution channel. Capping YSP and enhanced disclosure to the American Consumer that their third-party originator is being additionally compensated by providing a higher than market interest rate, will assist in keeping/precluding borrowers from taking loans with pre-payment penalties that tend to lock borrowers into programs they probably should not have taken to begin with.

ACUMA agrees that limiting a pre-payment penalty to an initial fixed rate period is an excellent idea especially for programs where the initial fixed rate period is artificially low and/or only remains for a very short period of time as an alternative to completely outlawing pre-payment penalties.

Respectfully submitted on behalf of the American Credit Union Mortgage Association,

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