CBA | CONSUMER BANKERS ASSOCIATION

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Re: **Proposed Statement on Subprime Mortgage Lending; 72 Fed. Reg. 10533 (Mar. 8, 2007)**

Ladies and Gentlemen:

The Consumer Bankers Association ("CBA")[1] appreciates the opportunity to comment on the Proposed Statement on Subprime Mortgage Lending ("Statement") issued by the

[1] The Consumer Bankers Association 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

Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and the National Credit Union Administration ("Agencies").

Summary

CBA supports the general principles expressed in the Statement as follows:

"Fundamental consumer protection principles relevant to the underwriting and marketing of mortgage loans include:

- Approving loans based on the borrower's ability to repay the loan according to its terms, and
- Providing information that enables consumers to understand material terms, costs and risks of loan products at a time that will help the consumer select products and choose among payment options."

We agree that consumers need to be protected from unscrupulous loan originators who prey on the more vulnerable consumers in our society. Accomplishing that, however, requires that these principles be expressed in regulations applicable to all loan originators, not just to regulated financial institutions. Otherwise, they will not protect consumers from the very actors from whom they are most in need of protection.

At the same time, it is important not to go too far and unduly restrict access to credit. The home ownership rate in America is at an all time high and we would like to keep it that way and expand it for minorities. We do not want to see restrictions that create a return to the days when many people were unnecessarily closed out of the community of homeowners. Limiting the coverage of the Statement to subprime mortgages is therefore critical, as is maintaining a flexible approach to the provisions enunciated in the Statement.

We agree with the Statement that loans should be made based on the assessment of the borrower's ability to repay. They should not be made based on collateral value (a principle enunciated by the OCC in National Bank Act regulations), nor (as the Statement says) should loans be based on the expectation of repeated refinancing.

We also support the principle expressed in the Statement that increased risks need to be properly underwritten. However, most of the products and loan terms to which the Statement refers are not *per se* predatory. They can serve the

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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.

needs of some customers while not serving the needs of others. We recognize that subprime borrowers are often more vulnerable to shifts in payment amounts caused by market forces or loan terms. As a result, more conservative underwriting protections are necessary.

We strongly support improving and streamlining disclosures to make the terms of mortgage loans more understandable to the consumer. We agree that information should be provided early as a shopping tool, when possible. However, improving disclosures does not mean layering additional information onto existing disclosures, but streamlining and simplifying so consumers have the most important information in a readily understandable form. It is also critical that disclosures be uniform in content, consistent in presentation, and mandatory for all lenders.

We believe this Statement is not the proper vehicle for improving disclosure requirements. It is neither uniform in application, nor specific in its terms. It speaks in general terms of the need to ensure that the consumer understands the loan features and risks, but it does not provide specific content nor dictate the delivery process. Without such specifics, the disclosures will fall short of achieving their purpose.

TILA and RESPA regulations should be amended to address these disclosure needs. In that way, all lenders would be subject to requirements that are uniform, effective and certain, and consumers would be provided with the information they need.

In the final analysis, however, even the best disclosures are only useful to a relatively well-educated consumer of these products, because they are attempting to describe complex financial transactions that are not easy to understand. A financially educated populace is a better deterrent to fraud and predation than any amount of federal regulation. That is why, at CBA, we join our member banks in encouraging more and better financial education initiatives in school curriculums and in the communities.

Major Considerations

<u>Uniform Application</u>
The Statement should apply uniformly to all mortgage lenders.

Currently, the Interagency Statement applies only to regulated depository institutions and their affiliates. Footnote 6 states:

> As with the *Interagency Guidance on Nontraditional Mortgage Product Risks*…this Statement applies to all banks and their subsidiaries, bank holding companies and their nonbank subsidiaries, savings associations

and their subsidiaries, savings and loan holding companies and their subsidiaries, and credit unions.

We believe that this will not get to the root cause of most of the problems and will have unintended consequences.

The subprime loan market often operates below the federal regulatory radar screen. Although bank lenders are subject to bank regulatory standards, mortgage brokers and loan officers in non-bank companies are not subject to federal enforcement of lending laws. Rather, states have the primary enforcement responsibility for regulating these mortgage brokers. State-chartered mortgage brokers and nonbank affiliates underwrote approximately 77 percent of subprime loans in 2005.[2]

More important, even those that are being made by covered institutions are, for the most part, not the ones most in need of this increased scrutiny.

Banks and thrifts are already subject to an array of additional rules and guidelines that are carefully crafted to prevent their engaging in predatory lending, and which are enforced through the rigorous oversight process unique to banking.

For example, the bank regulatory agencies (OCC, OTS, FRB and FDIC) on January 31, 2001, issued Expanded Guidance for Subprime Lending Programs.[3] In pertinent part, the Guidance states:

> The term subprime is often misused to refer to certain "predatory" or "abusive" lending practices. The Agencies have previously expressed their support for lending practices designed to responsibly service customers and enhance credit access for borrowers with special credit needs. Subprime lending that is appropriately underwritten, priced and administered can serve these goals. However, the Agencies also recognize that some forms of subprime lending may be abusive or predatory. Some such lending practices appear to have been designed to transfer wealth from the borrower to the lender/loan originator without a commensurate exchange of value…. Typically, predatory lending involves at least one, and perhaps all three, of the following elements:
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> - Making unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation;

[2] Special Report by the Joint Economic Committee, Sen. Charles E. Schumer (D-NY), Chairman: Sheltering Neighborhoods from the Subprime Foreclosure Storm, 2007 (footnote omitted).
[3] Expanded Guidance for Evaluating Subprime Lending Programs – FIL-9-2001, January 31, 2001: http://www.fdic.gov/news/news/financial/2001/fil0109.html

- Inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced ("loan flipping"); or
- Engaging in fraud or deception to conceal the true nature of the loan obligation, or ancillary products, from an unsuspecting or unsophisticated borrower.

> <u>Loans to borrowers who do not demonstrate the capacity to repay the loan, as structured, from sources other than the collateral pledged are generally considered unsafe and unsound. Such lending practices should be criticized in the Report of Examination as imprudent. Further, examiners should refer any loans with the aforementioned characteristics to their Agency's respective consumer compliance/fair lending specialists for additional review.</u> *Emphasis added.*

The Community Reinvestment Act (CRA) also prohibits depository institutions subject to CRA from obtaining favorable CRA consideration for loans that are illegal or discriminatory. On July 12, 2001, the CRA Q&A was revised to clarify that an institution engages in discriminatory credit practices if it discourages or discriminates against credit applicants or borrowers on a prohibited basis, in violation, for example, of the Fair Housing Act or the Equal Credit Opportunity Act (as implemented by Regulation B). It further provides that loans that are unfair or deceptive are not eligible for favorable CRA consideration.

The OCC and the FDIC have provided additional guidelines on predatory lending.[4] In 2003, the OCC issued an Advisory on Predatory Lending, OCC AL 2003-2. More recently, the FDIC issued a Supervisory Policy on Predatory Lending, FIL-6-2007.[5]

National Banks have their own unique rules that are designed to ensure that they are above reproach when it comes to illegal or predatory lending practices. In February 2003, the OCC issued two releases establishing nationwide guidance to guard against predatory lending practices among institutions it supervises.

In two separate letters to national banks, the OCC stated that abusive lending practices may present significant safety and soundness problems or may involve unfair and deceptive practices in violation of the Federal Trade Commission Act.

The advisory letters emphasized that national banks should have policies and procedures in place to ensure that neither they nor their subsidiaries engage in

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[4] http://www.occ.treas.gov/ftp/advisory/2003-2.pdf

[5] http://www.fdic.gov/news/news/financial/2007/fil07006.html

any practices that might be considered predatory, and that their lending complies with safety and soundness standards and consumer protection laws.

The Comptroller said that while the OCC has no reason to believe that any national bank is engaging in predatory lending, the agency's guidance will help prevent problems from arising in the future by prescribing steps national banks should take to avoid abusive practices.

The guidance emphasizes that the OCC will review credible evidence that a national bank has engaged in abusive lending practices. If the bank is found to have violated an applicable law or safety and soundness standard, the OCC will take appropriate supervisory action.

Subsequently, on January 7, 2004, the OCC amended its rules under the National Bank Act to add two provisions designed to provide an additional layer of protection for consumers. One provision provides that a national bank may not make consumer loans based predominantly on the foreclosure or liquidation value of the borrower's collateral. This places a total ban on any lending by a national bank that does not take into consideration the borrower's ability to repay, a ban on loans made with the expectation of profiting from foreclosure. The second provision added to the new rules states that a violation of section 5 of the FTC Act, which protects consumers against unfair or deceptive acts or practices, is a violation of the National Bank Act. This ensures that the OCC can employ its enforcement authority against banks that engage in any unfair or deceptive practices as defined by that act, and maintain its vigilant oversight to prevent predatory lending practices of any kind.

Thus, the need for this Statement is least where it applies and most where it does not. By enforcing stricter standards on some lenders, it risks driving consumers to those who are least regulated and least scrutinized. The impact on the communities could be detrimental, since it will leave vulnerable consumers unprotected where protection is most needed.

Although we support the efforts of the states through the Conference of State Bank Supervisors to adopt parallel rules for non-bank affiliated state licensed lenders and brokers, state adoption of comparable codes will not ensure uniformity. **A true level playing field calls for federal regulation under one or more existing laws that would apply to all mortgage lenders. The best regulatory approach will depend on the terms being considered, and we would be happy to participate in any discussion going forward to determine what would be most effective.**

<u>Subprime only</u>

The Interagency Statement should be limited to <u>subprime</u> mortgages only.

Prime borrowers are less vulnerable than subprime borrowers, and the problems for which the Statement was drafted do not seem to be present in the prime markets. For example, the foreclosure rate for prime mortgage has remained constantly low, while the subprime rate has climbed and is predicted to rise further. Because the Statement will have the effect of reducing availability of credit, we should be extremely cautious about expanding it beyond what is strictly necessary. Neither prime loans nor jumbo loans should be included under the Statement.

The definition of "subprime" being proposed in the Statement, however, is not very practical for lenders to use**.** It is based on *the 2001 Expanded Guidance for Subprime Lending Programs*, where it states:

> The term 'subprime' refers to the credit characteristics of individual borrowers. Subprime borrowers typically have weakened credit histories that include payment delinquencies, and possibly more severe problems such as charge-offs, judgments, and bankruptcies. They may also display reduced repayment capacity as measured by credit scores, debt-to-income ratios, or other criteria that may encompass borrowers with incomplete credit histories. Subprime loans are loans to borrower displaying one or more of these characteristics at the time of origination or purchase. Such loans have a higher risk of default than loans to prime borrowers. Generally, subprime borrowers will display a range of credit risk characteristics that may include one or more of the following:
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> - Two or more 30-day delinquencies in the last 12 months, or one or more 60-day delinquencies in the last 24 months;
> - Judgment, foreclosure, repossession, or charge-off in the prior 24 months;
> - Bankruptcy in the last 5 years;
> - Relatively high default probability as evidenced by, for example, a credit bureau risk score (FICO) of 660 or below (depending on the product/collateral), or other bureau or proprietary scores with an equivalent default probability likelihood; and/or
> - Debt service-to-income ratio of 50% or greater, or otherwise limited ability to cover family living expenses after deducting total monthly debt-service requirements from monthly income.
>
> This list is illustrative rather than exhaustive and is not meant to define specific parameters for all subprime borrowers.

This definition calls for a number of factors to be considered, and, as it states, the list of factors is only illustrative. Without greater certainty, lenders run too great a risk of noncompliance. To ensure compliance, they may extend the restrictions and prohibitions beyond the necessary markets, thus overly restricting credit availability. Loans subject to the provisions of the Statement need a clearer delineation, a bright line test that would be easier for lenders to employ. We suggest using an existing and widely employed measure, such as the HMDA threshold. While not a perfect measure of everyone's idea of subprime (no such measure exists), it would at least be a standard that is widely recognized and already in use. In any case, we suggest that some clearer threshold be established than the one proposed in the Statement.

<u>Underwriting subprime hybrid ARMs</u>

We support the principle that subprime hybrid ARMs with short times to the first reset be underwritten to the "fully indexed rate."

The Statement says, "prudent qualifying standards recognize the potential effect of payment shock in evaluating a borrower's ability to service debt. An institution's analysis of a borrower's repayment capacity should include an evaluation of the borrower's ability to repay the debt by its final maturity at the fully indexed rate, assuming a fully amortizing repayment schedule."

We believe that if a subprime hybrid ARM product has a short initial reset period, such as the popular 2/28 and 3/27 products, the underwriting of the ability to repay should be determined using the fully indexed rate, assuming a fully amortizing repayment schedule.

Loans with longer initial fixed rate terms, such as 5/1's, should not be subject to the same standards. The amount of time that would elapse between the closing and the reset is long enough that predicting the index on which the rate will be determined is not meaningful. Nor can the lender reasonably forecast the consumer's income or circumstances so many years hence.

It is worth noting that this is one of the few examples in the Statement where no flexibility is accorded to the lender. The basis of the Statement's approach to guidance is to ensure that lenders undertake prudent underwriting and avoid layering risk factors, no one of which, alone, necessarily creates a problem. In this case, however, the expectation that lenders underwrite to the fully indexed rate appears to allow for no mitigation or offset. While it may appear axiomatic that lending based on an ability to repay is equivalent to underwriting to the fully indexed rate, the Statement does not make the case. It may prove that some of the other identified risk factors, individually or collectively, have a greater correlation with default than underwriting to the starting rate on a hybrid ARM. [6]

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[6] In the recently issued *Interagency Guidance on Nontraditional Mortgage Product Risk*, the Agencies allow for alternatives. Footnote 5 of the Guidance states in part: "In different interest rate scenarios, the fully indexed rate for an ARM loan based on a lagging index (e.g., MTA rate) may be significantly different from the rate on a comparable 30-year fixed-rate product. In these cases, a credible market rate should be used to qualify the borrower and determine repayment capacity."

<u>Taxes and Insurance</u>

The Statement further states, “An institution’s DTI analysis should assess a borrower’s total monthly housing-related payments (e.g., principal, interest, taxes, and insurance, or “PITI”) as a percentage of gross monthly income.” We fully support this principle. We are gratified that the Statement does not attempt to mandate any particular ratio as permissible. Too many variables affect the most appropriate ratio lenders choose to employ.

<u>Treatment of Brokers</u>

We believe that mortgage brokers need improved licensing, disclosure and regulatory oversight and enforcement.

Mortgage brokers require a national process of licensing and regulation, and should be subject to a bonding or net worth requirement. In addition, state or federal regulators should enhance uniform regulatory oversight programs of mortgage brokers. It should not be the role of financial institutions or the secondary market to “police” independent brokers for compliance.

<u>Stated Income and Low Doc/No Doc lending for Subprime Mortgages</u>

We generally support the treatment of Stated Income and Reduced Documentation Lending in the Statement.

Stated income and reduced documentation lending, in concert with other factors such as high LTV, may have contributed to some of the subprime problems we are currently experiencing. As such, it is appropriate that the agencies look carefully to determine what risks are involved for consumers and lenders. Stated income and reduced documentation lending can be useful and should not be prohibited outright. In the case of subprime loans, we support the position expressed in the Statement:

--An institution should have clear policies governing the use of reduced documentation loans; and

--The higher the loan risk, the more important it is to verify the borrower’s income, assets and liabilities.

The Statement calls for “mitigating factors” when reduced documentation is employed in higher risk loans. It would be helpful if examples of such mitigating factors were provided. A consumer well known to the bank, a wealthy applicant with an abundance of legitimate secondary sources of repayment, or similar situations, for example, may warrant the use of stated income. However, where mitigating factors are not present, institutions generally should employ the primary borrower’s recent W-2 statements, pay stubs or tax returns, when they are obtainable. If more than one is available, however, it should not be necessary to review them all.

When stated income or reduced documentation lending is employed notwithstanding documentation that may be available, we also support clear disclosure of the additional cost, if any, that this would entail for the consumer.

Incentive compensation

Incentives should never be structured to encourage unsound underwriting or illegal, discriminatory steering.

The Statement provides, "Institutions should design compensation programs that avoid providing incentives for originations inconsistent with sound underwriting and consumer protection principles, and that do not steer consumers to these products to the exclusion of other products for which the consumer may qualify." We agree that institutions should avoid any practices inconsistent with sound underwriting and consumer protection principles.

However, in the context of this Statement, this principle might be mistakenly viewed as a prohibition against compensation programs that appear to encourage hybrid ARMs, rather than 30-year fixed rate mortgages, without otherwise considering the effect on sound underwriting or consumer protection principles. Incentive compensation, per se, is not a problem, provided loans are made based on an ability to repay, are responsibly underwritten, and provide strong consumer protections and full disclosures. Subprime hybrid ARMs—if they are made safely and responsibly—can make it possible for more people to obtain equity financing or purchase a home. Financial institutions that are seeking to reach out into new markets, markets that have not had sufficient access to credit in the past, often employ incentives to the broker or loan officer. The problem is not compensation, but forms of lending without consideration of the ability to repay. Ensuring that such products are only offered responsibly resolves the underlying problem.

It is not the role of the lender to determine if a product is appropriate or suitable for the borrower. It is the lender's responsibility to make a reasonable determination of whether the borrower has the ability to repay the loan. Beyond that, the choice of products and terms should be the borrower's. Few consumers would want the choice of products and terms to be stripped from them because the lender is concerned about the suitability of the product.

Disclosures

Current disclosures are not adequate, but the Statement does not offer a practical alternative. Existing regulation should be amended to improve disclosures.

The language of the Statement includes many places where it calls for the lender to provide clear, detailed information about costs and product features. Yet specifics appear to be left to the institutions to develop.

For example, the Statement says:

- Institutions are required to provide "information that enables consumers to understand material terms, costs, and risks of loan products at a time that will help the consumer select products and choose among payment options."

- "[C]ommunications with consumers, including advertisements, oral statements, and promotional materials should provide clear and balanced information about the relative benefits and risks of the products."

- "This information should be provided in a timely manner to assist consumers in the product selection process, not just upon submission of an application or at consummation of the loan."

- "Institutions should not use such communications to steer consumers to these products to the exclusion of other products offered by the institution for which the consumer may qualify."

- "Information provided to consumers should clearly explain the risk of payment shock and the ramifications of prepayment penalties, balloon payments, and the lack of escrow for taxes and insurance, as applicable."

  [*A footnote to this statement says*: "To illustrate: a borrower earning $36,000 per year obtains a $200,000 "2/28" mortgage loan. The loan has a two-year introductory fixed interest rate of 7%, resulting in an initial payment of $1,331 and a 44% debt-to-income (DTI) ratio, based on principal and interest only; and would be higher after the inclusion of taxes and insurance. The spread is 6% over the six-month London Interbank Offered Rate (LIBOR), which is 5.5% at the time of loan origination. The fully indexed interest rate at origination of 11.5% (6% + 5.5%) would cause the borrower's monthly payment to increase to $1,956 (or 47%), a 65% DTI ratio, based on principal and interest only." Fn. 10]

- "[M]ortgage product descriptions and advertisements should provide clear, detailed information about all of the costs, terms, features, and risks of the loan to the borrower. Consumers should be informed of:

1. Payment Shock. Potential payment increases, including how the new payment will be calculated when the introductory fixed rate expires.
2. Prepayment Penalties. The existence of any prepayment penalty, how it will be calculated, and when it may be imposed.
3. Balloon Payments. The existence of any balloon payment.
4. Cost of Reduced Documentation Loans. Whether there is a pricing premium attached to a reduced documentation or stated income program.
5. Responsibility for Taxes and Insurance. The requirement to make payments for real estate taxes and insurance in addition to their loan payments, if not escrowed, and the fact that taxes and insurance costs can be substantial."

These are reasonable principles, and we support them as general goals. Disclosures that are currently provided to consumers in mortgage lending transactions may be inadequate to the needs of the more complex products of recent vintage and should be reviewed and improved. However, this Statement is an inadequate means to eliminate these shortcomings, for several reasons.

First, since the Statement applies only to some lenders, as noted above, any new disclosures would be provided only by covered institutions—a minority of the lenders for whom they are most necessary.

Second, because the standards being describe lack specific required disclosures at specific times, the information provided to the consumer would not be uniform from lender to lender –even among those who are covered by this Statement. Consumers who are shopping for credit need to have standard disclosures that they can compare from lender to lender. Even supposing that lenders all develop disclosures that, individually, meet the requirements of the Statement, consumers would be confused by the myriad ways in which the information is provided.

Finally, the Statement puts lenders in the position of having to develop ideal disclosures and advertisements, which are sufficiently "clear" and "balanced" to enable consumers to understand material terms, costs and risks. This is a desirable goal, but it is not an effective set of rules by which lenders can develop compliance policies and procedures. It is too subjective to be useful. What is clear and balanced or understood by the consumer depends on too many circumstances. It is also extremely difficult to explain clearly these complex mortgage transactions. The example in footnote10 shows how hard it is to provide such information; we suspect the typical consumer would not understand it. Developing a good, clear and concise set of disclosures should be the role of those developing regulations, employing consumer focus groups and other means of ensuring that consumers will understand. Even the call to provide information early enough to be useful as a shopping tool calls for a balancing: The earlier the information is given, the less specific it can be.

Currently, TILA and RESPA offer an abundance of disclosures of loan terms and provide much of the information necessary for consumers need in order to understand the transactions. TILA was developed precisely in order to create a uniform set of disclosures so consumer can compare creditors' rates and terms. We recommend making improvements to the regulations under TILA and RESPA to provide the best disclosures possible. By doing so, we would (a) avoid layering additional disclosures onto the existing ones; (b) create a set of streamlined and effective disclosures to replace the current ones; and (c) provide disclosures that would be given by all mortgage lenders, not just banks.

The terms of mortgage loans can confuse many consumers, but disclosures are not the only answer. Ideally, we need a national effort to expand consumer awareness of credit through financial education. Most banks are already engaged in financial education efforts. We encourage others to join in the effort, and particularly to take steps to encourage school systems to include financial education on their curricula.

<u>Questions</u>

(1) The proposed qualification Standards are likely to result in fewer borrowers qualifying for the type of subprime loans 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 payment risks to lenders or borrowers that should be discouraged, or alternatively, when and under what circumstances are they appropriate?

Such loans do not always present inappropriate risks. These subprime products were developed to expand access to credit. Although they have enhanced the risks for some consumers, and they have been sold to some consumers inappropriately, it is important to recognize that there is nothing fundamentally wrong with most such products. The payment risks are characteristics of the circumstances, not the products. Subprime hybrid ARMs can be wonderful choices for many families. Reduced documentation loans can permit those who are self employed or those with strong financial situations quickly to get a mortgage without complications. If the consumers are informed of the risks, these can be extremely beneficial.

(2) ***Will the proposed Statement unduly restrict the ability of <u>existing</u> 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.

We doubt there will be one solution to this problem. It will take many approaches working together to get consumers out of their difficulties. In the end, it will require both flexibility and creativity. Institutions do not want loans they are servicing to go into foreclosure, and so they are generally willing to be flexible in workouts and forbearance. Recently, a number of banks have announced special programs to deal with this situation, and others may do the same. The FFIEC has encouraged such action and offered CRA credit for those who participate. Other possible approaches that have been suggested may have promise. FHA reforms may permit FHA insured loans better to meet the needs of some of these consumers. The GSEs have suggested that they may be able to play a role.

Working together, financial institutions, consumer groups, and governments can do much to help in this area. Senator Dodd's Homeownership Preservation Summit Statement of Principles, endorsed by a number of CBA member banks along with many others, is an example of one such approach. These are all steps toward a solution.

We believe that the market place will be responsive to the need for alternative products that offer less opportunity for payment shock. If they exist, someone will find a way to make them available. Improved education, improved disclosure, and preventing the unnecessary layering of risk, remain important parts of any solution as well.

Nevertheless, if forecasts prove accurate, a great many consumers may have obtained loans that they will have a hard time repaying after the rate resets over the next few years. Those who may be hoping to refinance at the first reset could find themselves cut off by stricter lending requirements such as those enunciated in the Statement. We join others in our concern that those consumers who got into these mortgages without understanding the risks not be forced into foreclosure by a more restrictive lending environment that was not in effect at the time they obtained their loans. The net effect of the Statement as proposed would be to push the most at risk subprime borrowers towards unregulated companies to mitigate higher payments when their ARMs reset. Therefore, the Statement should be clarified to provide some discretion for institutions to refinance existing subprime borrowers under more flexible terms, when necessary.

(3) Should the principles of this proposed Statement be applied beyond the subprime ARM market?

No. The need for changes to underwriting requirements, in particular, as well as risk management and controls for prime loans is not evident based on any measure of data including delinquency or foreclosure trends. Prime borrowers are well served by flexible underwriting for a range of options, and have no need for such restrictions.

(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 relating 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.

We support the thrust of the Statement, to encourage penalties that are not excessive and that expire before the first reset on hybrid ARMs, so that consumers have an opportunity to refinance if necessary.

When structured fairly, prepayment penalties allow lenders to offer lower rates or fees on subprime loans, yet still recoup origination costs. Thus the rate offered to the consumer is related to the penalty that encourages consumers to stay in their loans. In short, penalties lower the initial cost to the consumer. Regulation in this area should be to ensure that consumers understand the risk associated with the trade off.

However, that paradigm changes if consumers who are faced with "payment shock" at the first reset on a hybrid ARM cannot refinance without facing a substantial penalty. The Statement therefore expresses concern about "substantial prepayment penalties" and strongly encourages institutions that impose them not to extend them beyond the initial reset period and to provide a sufficient window of time for the borrower to refinance without penalty. We support this cautionary note and appreciate the flexibility that it accords the lender. To the extent that subprime loans are made based on an ability to repay and properly underwritten, the concern about "payment shock" at the first reset is considerably ameliorated. Therefore, the trade off that might permit the consumer to obtain financing at a lower rate becomes a sensible financial choice in more cases.

Thank you for permitting us to comment on this Statement. If you have any questions, please do not hesitate to contact us.

Very truly yours,

/s/

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