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The Honorable Ben. S. Bernanke
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Board of Governors of the
Federal Reserve System
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Washington, DC 20551

The Honorable Mary L. Schapiro
Chairman
Securities and Exchange Commission
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The Honorable Shaun S. Donovan
Secretary of Housing and Urban Development
Department of Housing and Urban Development
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The Honorable Sheila C. Bair
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Ladies and Gentlemen:

We appreciate the work the agencies are doing to formulate the regulations necessary to effectuate the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Act). Of particular importance are the risk retention provisions of section 941, including the exemption for mortgages satisfying the "qualified residential mortgage" (QRM) requirements to be established by the agencies. We write to share our views concerning those requirements.

The credit risk retention rules should set the standards for the entire secondary market in residential mortgage loans. As appropriate for all mortgage loans, these rules should include standards for responsible loan origination. Additionally, they should include standards for responsible loan servicing, particularly for loans that become delinquent. The current foreclosure crisis has revealed that securitized loans give rise to a particularly difficult set of problems in servicing delinquent loans, and these problems increase the default and foreclosure risk associated with these loans. Accordingly, we believe that the risk retention rules should include both origination standards and servicing standards.

In setting out origination standards, we recognize the need to balance sound underwriting against current market realities. For example, with real estate values significantly depressed and not yet stabilized, setting appropriate loan-to-value ratios may be close to impossible for all consumers. Moreover, for communities of color and residents of traditionally underserved communities, it is even more important to permit flexibility in applying underwriting standards to take individual circumstances into account. We believe that it would be a mistake for QRM standards to create or reinforce a dual credit market in which the private market primarily serves white borrowers while communities of color are primarily served by FHA. For these reasons, we encourage the agencies not to establish firm LTV or DTI limits in the QRM. Nor do we support requiring through regulation the use of mortgage insurance on any loan.

Instead, we believe the QRM should act in concert with the Qualified Mortgage (QM) definition in Title XIV of the Dodd-Frank Act to establish standards for sustainable mortgage products that will serve the broad needs of consumers in a variety of circumstances. The key features of the QM definition that should be replicated in the QRM are:

- no negative amortization or deferred principal repayment
- no balloon payment (with limited exception)
- verified and documented ability to repay
- underwriting for fixed rate loans based on fully amortizing payments, including property insurance, taxes (PITI) and assessments; underwriting for adjustable rate loans at the maximum monthly payment allowed during the first 5 years based on fully amortizing payments including PITI
- compliance with points and fee limits
- maximum term of thirty years

The Board (and later the CFPB) also has the authority to set DTI or residual income guidelines as part of the QM definition. If the Board does so, it would be particularly confusing and detrimental to the market to have two potentially conflicting sets of requirements. Given the different rulemaking timelines, we suggest creating a standard in QRM that for now would tie any QRM DTI or residual income requirements to any standards that may ultimately be set in the QM.

Additionally, we suggest that the QRM definition exclude loans that carry a prepayment penalty. Title IX expressly authorizes the regulators to consider prohibiting prepayment penalties as part of the QRM definition. Prepayment penalties are known to increase the risk of default on a mortgage, and for this reason we suggest that no securitized mortgages carry them.

Next, we recommend that all securitized mortgages meet certain servicing standards. It is now well understood that the process of servicing securitized mortgages is rife with complications, from meeting the needs of all tranches of investors to obtaining permissions for needed changes to potential conflicts of interests with servicers owned by large banks. It is therefore crucial for the risk retention rules (including the QRM definition) to include the following requirements for all mortgages sold to investors as part of a security:

1. Servicers must mitigate losses by taking appropriate action to maximize the net present value of the mortgages for the benefit of all investors (rather than any particular investor class), and must pursue loss mitigation rather than foreclosure where doing so yields a net present value that is equal or greater.

2. The structure of servicer compensation schemes must not operate to encourage foreclosure over loss mitigation.

3. Servicers must implement a reasonable process for addressing subordinate liens owned by the servicer or any of its affiliates. The interests of the first lienholders on the property should have priority in the resolution of a troubled loan, and servicers holding second liens should have an absolute fiduciary responsibility to act in the best interests of the first lienholders, regardless of the servicer's other interests in the property. To facilitate these objectives, servicers must publicly disclose their ownership interests (or those of any affiliate) in any other loans secured by the property that secures any loan in the pool.

These standards should be set out in detail in the pooling and servicing agreement or other governing securitization document. They also should be set out as covenants in the mortgage note and loan agreement to facilitate compliance.

We appreciate your consideration of our views and are happy to provide any further information that would be helpful.

Sincerely yours,

Michael Calhoun
President, CRL

Barry Zigas
Director of Housing Policy
Consumer Federation of America

Willard Ogburn
Executive Director
National Consumer Law Center
(on behalf of its low-income clients)

Ira Rheingold
Executive Director
National Association of Consumer Advocates