Community Spirit
BANK®

October 2, 2012

To: Board of Governors of Federal Reserve System
Jennifer J. Johnson,
Secretary, Board of Governors of Federal Reserve System
Docket No. R-1443
RIN 7100-AD90
Via email to regs.comments@federalreserve.gov

Bureau of Consumer Financial Protection
Monica Jackson
Office of the Executive Secretary
Docket No. CFPB-2012-0031
RIN 3170-AA11
Via Electronic Submission at www.regulations.gov

Federal Deposit Insurance Corporation
Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Housing Finance Agency
RIN 2590-AA58
Via email to comments@fdic.gov

Re: Comment Letter on Appraisals for Higher-Risk Mortgage Loans

I appreciate the opportunity to write to you regarding the proposed new appraisal requirements for "Higher Risk Mortgages". I am President/CEO of Community Spirit Bank, chartered in 1908 in Franklin County, City of Red Bay, Alabama. We have a long history of helping consumers in our communities obtain their dream of homeownership. Our residential loans comprise of a quarter of our loan portfolio and from that vantage point, we feel we have the experience and expertise to comment on the proposed rules with regard to "Higher Risk Mortgages".
It is my understanding that regulatory officials continue to implement aspects of the Dodd-Frank Wall Street Reform and Consumer Protection Act and the proposed rule regarding appraisals and High Priced loans would be revised as a part of that Act. I want to write to you to let you know how this will affect my bank and the consumers in which we serve. I realize you have asked for specific questions to be answered in the comment period and I will try to answer some of them, but I do want to make comments outside of your questions.

First, all 1-4 family, closed-end consumer driven real estate loans made by my bank are considered "high priced" based on regulatory definitions. My bank holds our mortgages in-house from origination to payoff. We underwrite these loans with the intention of having to "live with them" for the life of the loan. We were in complete disagreement with changes of Regulation Z that required my community bank to underwrite loans I originate and keep for the life of the loan to be considered "high priced" and thus having the escrow requirement. We strongly believe this regulation took a differentiation advantage we had over mortgage companies away from us. Further, this severely hampered our ability to generate these 1-4 family loans. To demonstrate, I want you to see real life numbers.

Let me illustrate to you the following information, which is our 1-4 family loans originated in the following years

Year	# of Loans Originated	$ of Origination
2007	34	$ 1,612,588.37
2008	82	$ 4,955,616.60
2009	140	$ 11,134,628.17
2010	77	$ 5,076,172.25
2011	75	$ 4,983,701.67
9 MONTHS 2012	55	$ 4,498,264.94

The escrow requirement took effect on April 1, 2010. We believe this law as enacted is the reason our 1-4 Family loan originations declined sharply as the revised rules from April 1, 2010 made it much more difficult to approve loans to borrowers and it made it more difficult for borrowers to qualify for loans to purchase residences.

In addition, the following are year-end totals of our 1C2A portfolio as a whole: As you can see, our portfolio hit a high in 2009, but began shrinking in the years since that time. We have made some increases in the loan balance owed but still not to the level we were prior to the current changes to Reg Z that became effective in April 2010.

Year	1C2A Portfolio	Loan Portfolio	% OF PORTFOLIO	
2007	**$ 18,425,256.87**	$ 77,416,964.45	23.80%	
2008	**$ 17,742,824.63**	$ 82,765,960.85	21.44%	
2009	**$ 22,427,049.87**	$ 87,981,548.02	25.49%	
2010	**$ 21,804,441.77**	$ 88,394,966.38	24.67%	
2011	**$ 21,668,628.95**	$ 85,419,976.99	25.37%	
2012 9 months	**$22,021,218.36**	$ 88,438,081.32	24.90%	

So, as you can see; my 1-4 Family portfolios has shrunk in our opinion, as a result of the differentiation factor the changes to Regulation Z took away from our bank. The regulation

requires our bank to compare our loan that we will hold until payoff against the "national average prime offer rate" and if we are above the thresholds as described in the regulation we must escrow. You can see that we believe this has already had a negative effect on our financial institution and the consumers in which we serve. We have lost both number and dollar amount of originations since the law took effect and our portfolio as a whole shrunk but has increased some during this year, but still not to where we was at the high of 2009.

The effect on the consumers is not as easily measurable, but I can tell you some facts. Prior to the changes to Reg Z, we would require customers to come to the closing table with 10% down. Now, the down payment is upwards of 13% or higher because the consumer now has to come to the table with the first year's taxes and insurance in addition to the down payment. It was difficult enough for customers to arrive at the table with the 10% down, but now requiring first years taxes and insurance is a double burden on these consumers and resulted in less loans originated by my bank. Further, consumers who already owned their home, but hoped to refinance and obtain new money to purchase something else, using their home as collateral found that the amount of money they were able to "walk away from the table" with shrunk because we were having to deduct for taxes and insurance. In rural communities the vast majority of our residential loan customers don't have the financial capability to pay all their insurance up front for the entire year. Let me give you an example of the implications this regulation has already had our borrowers:

> Borrower Purchases a House for $100,000.00. Must pay 10% down which is $10,000.00. Borrower has to get insurance in place on house. Borrower can't afford to pay the $800.00 per year premium up front, so the insurance company allows them to pay it over 12 months. The bank also has to have the customer pay into the escrow account and start building for the next year. So, Borrower has a principal, interest, taxes and insurance payment to bank and borrower also has payment to insurance company. This is how this regulation is affecting our customers. They are being "double hit" in that first year. The proposed rules do nothing to cure this current problem and now the regulation will add another appraisal cost. We believe that banks such as ours that hold and service a loan for its life should be exempt from burdensome regulations such as the changes to Regulation Z from April 2010 as well as the proposed changes.

The reader may believe that our bank simply should simply choose to price our loans below the "average prime offer rate" (APOR) to keep from having to escrow and be subject to the proposed rules regarding appraisals. I would respectfully disagree. We have and continue to feel that we have **three** risks in pricing our loans below this "average prime offer rate".

The first was interest rate risk. Our margins would have been squeezed to thin and we would have obtained much greater interest rate risk if we would price loans below this threshold. For instance, as of this writing, I priced a loan to a consumer on their dwelling today and my rate would have had to have been reduced by .23% to just be at 1.50% above the APOR. We believe we know our market, our cost of funds, and our overall interest rate risk better than a website comparing all current offering rates including those who may not hold their mortgages for the life of the loan, thus we choose to price our loans based on what is best for our financial institution and not let government dictate the price we charge.

Secondly, the APOR gives no credence to the differences in Loan to Value or other "Credit Risk" thresholds. The APOR does nothing to account for these other inherit risk including adequately funding of the ALLL etc. To compensate for this pricing, we believe the bank should be allowed to price the loan without penalty from regulations of calling our loan, "high priced".

Third and finally, we feel there would be fair lending risk in arbitrarily pricing loans below the APOR. For instance, it is our understanding that the APOR changes frequently and we would fear how fair lending examiners may review how we priced different loans to different borrowers on different days of the month or year as there would be no consistency in pricing loans. Thus, we believe this is too great of a fair lending risk for the bank to just arbitrarily pick a rate to be below the APOR.

You can see from this background that we have believed since the implementation of changes to Regulation Z in April 2010 that this would have a negative effect on our financial institution's 1-4 family mortgage program and we believe that it indeed has just that. It is with this background that we are very skeptical and concerned about the newest proposed changes being contemplated by regulatory officials with regard to appraisal requirements on "high priced loans".

Regulatory officials should consider that community banks like mine did not create the financial crisis that led to these proposed changes. We are not perfect, but we do believe that we are paying for the mistakes of the largest and most irresponsible financial institutions in the nation with these continued changes to how we make our 1-4 Family Residential loans. Some of our concerns with the proposed rule are as follows:

- At present, our state and federal law allows for the bank to perform in house evaluations on properties below $250,000.00 subject to certain requirements to be performed by the evaluator of the property and analysis on the property. Under current Alabama State Law, we can charge for these evaluations as well, which gives the bank good non-interest fee income and these evaluations charged by the bank are less expensive than certified appraisals, thus the consumer benefits from this as well. Under the proposed rules, this is in jeopardy of being changed.
- Every 1-4 Family loan we make is "High Priced" because we don't want to take the interest rate risk, thus we would have to comply with these new appraisal requirements
- We currently utilize conservative, in house evaluations, under the proposed rule; you require an appraisal to be performed by a "certified or licensed" appraiser. The consumer's we deal with will be disproportionally impacted because certified appraisals are 21% higher than our internal evaluations. We don't believe this is in the best interest of the consumer!
- It is our interpretation that not only does the regulation not allow for in-house evaluations, but also, it requires two (2) certified appraisals to be performed if "the seller is selling the property within 180 days prior to new loan" or when "the consumer is acquiring the home for higher price than seller paid". It is our understanding that the "second appraisal" will <u>not</u> be at the expense of the borrower, thus if the seller refuses to pay it, then to comply, the bank will be left to pay the bill. Thus, in our interpretation of this instance, this regulation takes our non-interest income away by not allowing us to use

an in house evaluation and then puts the bank at risk of an additional expense on the loan by having to pay for the "2nd appraisal". We are in strong disagreement with how this is written and the effect this will have on our customers and the bank.

- We have concern over requiring sellers to "prove" improvements made to property in short periods of time. We all know that foreclosures across our nation have been a big problem since 2008 and their remains a tremendous amount of inventory across our nation. Although our market area has weathered this downturn much better than other communities, we have concerns over the impact the regulation has on potential investors. We would ask what incentive does this regulation give to potential investors to purchase properties held in bank OREO inventories, make improvements to those properties and then sell those properties thus helping the economy and subsequently the housing market in general if they will have to have 2 appraisals to justify this approach and prove every dollar that went into the property. Further, how much of a profit is "too much" for a potential investor to make on turning a home. We believe the market dictates what a property is worth, not government regulations. We would strongly urge the regulatory officials to contemplate the implications this rule will have on disposing of housing inventories across the country.
- Consumers may choose to seek another lender who will take the interest rate risk and the fair lending risk just to price loans below the APOR. It would appear that these regulations are written in a way to penalize lenders who want to maintain safe and sound banking practices such as appropriately pricing a loan based on credit and interest rate risk by making them escrow and then throwing these new appraisal requirement rules on them as well.
- This new rule will encourage lenders such as ours to either exit the residential mortgage market are be forced to price loans as such low levels it would be risk prohibitive to continue in the residential mortgage market.
- We would strongly encourage regulatory officials to exempt community banks such as ours who serve in rural areas and maintain their loan portfolios in house for the life of the loan from both Escrow and new "appraisal requirements under Reg Z".

That concludes some of my general comments, and now, I would like to address some of the specific questions the proposed rule is seeking input upon:

- We believe the current appraisal requirements in place should remain in place and that the new appraisal guidelines if implemented only apply to those transactions that are greater than $250,000.00 in value. This answers question #1 from page 22 of the proposed rule.
- Question #5 from page 29, yes, we believe that there should only be one term used, not two so no further confusion exists, we believe if the regulations stand as written, one name "high priced mortgage loan" should be the correct term.
- Pages 38-42 of the proposed rule discusses "exemptions" available as well as Question #14 of "Classes of Loans" We find no mention of "excluding" rural lenders or community bank lenders who hold their residential mortgage loans in house for the life of the loan. We believe this should be an additional "exemption from the "higher priced mortgage loan" requirements. We would argue that our residential mortgage portfolio is as safe as any "reverse mortgage" or other "qualified mortgage" as described in these pages. We strongly request that regulatory officials provide an exemption for community

banks such as ours. We believe if a lender holds a loan for its life, they should be excluded from these requirements.

- Question #12: We would request that construction loans be excluded from the definition of "higher risk/priced mortgage loans". These loans have inherently greater risk than other loans and thus, should not be compared to other loans as each construction loan should be priced based on the risk it poises to the bank.
- Page 50 of the proposed rule again speaks that "the agencies are proposing to interpret the statute to expand appraisal requirements for higher risk mortgage loans of $250,000.00 or less, not just those above this threshold". We strongly voice our opposition to this interpretation. We believe that evaluations should continue to be acceptable for loans of $250,000.00 or less.
- Question #16: Whether you call it "additional appraisal" or "2nd appraisal", we believe this is a waste of someone's funds. The seller, buyer, or lender will have to pay for this additional appraisal. If the regulation stands as presented, we would be of the opinion it should be called "additional appraisal".
- Question #18 and #19: We believe throughout this letter, we have made it very clear that we would answer both of these questions by requesting that "rural banks" be exempted from the high priced mortgage and appraisal requirements. We hope the data provided at the beginning of this letter demonstrates the effect that the Escrow Requirement has already had on our financial institution and if another regulation goes into effect requiring more of both the lender and the borrower and now even the seller, the regulation will have a negative impact on the consumer and the economy in general. We strongly encourage rural lenders or those who hold loans in their portfolio to be exempted from these requirements.

  Further, it is very difficult to get appraisers in our area to obtain values based on comparable sales on properties, thus even if you require two appraisers, those appraisers are likely to be using the same "comparable sales", so what did we really gain?
- Question 20, 21, 22: It seems as though these new requirements and terms acquisition etc all revolve around trying to avoid "flipping fraud". From a rural banker's perspective, we can see no risk here anyway! We know our customers; we underwrite loans that we will service for the life of the loan. We are not going to loan someone money we don't know and thus, we would know if there was a "flipping scam" where one borrower sold another borrower money generated cash, then defaulted on the loan. With all the other new requirements of verifying income, applications etc., how could a local bank experience fraud? Further, with all the new appraisal rules over the past 5 years, the appraisals ordered independent of the loan officer, the buyer or the seller, thus from our perspective, the current appraisal regulations already take this aspect of fraud out of the equation.

Finally, I want to share with you my net loss experiences in our 1C2A portfolio over this same period of time. We have been very blessed with low loan losses in this category of loans primarily because we underwrite loans that we will "live with" for its entirety. Further, we know our customers, we know our sellers and like any bank will take our losses, but don't believe we will be taken as a victim of "flipping fraud". The below table list our loss experiences.

Call Code 1C2A Net Losses Per Year		
Year	$ Amount	% Amount
2007	$10,785.57	0.06%
2008	$33,822.26	0.16%
2009	-$5,306.65	0.00%
2010	-$5,306.65	0.00%
2011	-$2,488.51	0.00%
9 Months 2012	$5,650.69	0.03%

As you can see, by holding mortgages in our portfolio in house, using sound underwriting and "knowing our customers" we have had minimal losses in this segment of the portfolio. Thus, if this rule is simply to assist in avoiding flipping fraud that will lead to bank losses, we believe common sense underwriting and current appraisal regulations keep that from occurring.

Finally, to answer the final question in this section, we do believe that additional guidance should be given for those instances where a borrower inherits a property or buys out the remaining interest in a property they already own.

- Question #29. I believe the appropriate method should be a fixed percentage to determine the amount above what the seller gave for the property and I would suggest that the seller be allowed to make at least 25% if regulations are now going to dictate how much sellers can make on properties. Otherwise, you discourage investors from turning defunct houses around. However, I don't believe the lender or government regulation should dictate to someone who much profit they make off of selling a house so long as no fraud is involved and buyer and seller agree on price and appraisal justifies the price.
- Question #33: Our comment is that only one appraisal should be performed by an independent appraisal. If regulation requires these 2 appraisals, then regulation should define that one of the appraisals must be paid for by the seller, or that both must be paid for by the buyer. The lender should never have to pay for this additional appraisal. This leaves it for either the buyer or seller and in our opinion both appraisals are going to look the same in a rural area, thus, the second or additional appraisal is a waste.

As you can see from this letter, we strongly believe that a rural, community bank such as ours should be exempted from the requirements of this proposed rule. We believe that we do a good job of serving our communities. We underwrite loans that we will have in our portfolio for the life of the loan. We believe these proposed rules with further limit economic growth and further deteriorate our residential mortgage portfolio. We strongly encourage regulatory officials to consider exempting community banks from these requirements are at a minimum use the current language that continues to allow evaluations for transactions of $250,000.00 or less. Rules like this one being proposed will only further limit economic growth of our nation and our community and may even force community banks like ours out of the residential mortgage business altogether like many of my colleagues have already chosen to do. The choice seems clear, exempt community banks, the lifeblood of our nation's communities from burdensome regulations such as this.

Again, I appreciate the opportunity to write you regarding this matter and demonstrate to you the effects we believe this proposed rule will have on our bank and our consumers in which we serve. We respectfully request that you re-consider these rules based on the information we have presented to you in this letter.

Sincerely,

Brad M. Bolton
President/CEO/Sr Lender
Community Spirit Bank
FDIC Certificate #50
Red Bay, Franklin County, Alabama

Note: Financial data of Community Spirit Bank listed above was combining Community Spirit Bank, Red Bay, Alabama and Spirit Bank, Belmont MS, as Spirit Bank was merged into Community Spirit Bank on January 1, 2012, thus data for previous years was combining both banks as we had complete control of both banks and their underwriting and management of both portfolios and customers.

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