MORTGAGE BANKERS ASSOCIATION
Investing in communities

December 4, 2006

Office of the Comptroller of Currency
250 E Street, SW
Mail Stop 1-5
Washington, DC 20219

Ladies and Gentlemen:

Re: Comments in Response to Proposed Illustrations of Consumer Information for Nontraditional Mortgage Products: Department of the Treasury Docket No. 06-12 71 Fed. Reg. 58672, October 4, 2006.

The Mortgage Bankers Association[1] (MBA) greatly appreciates the opportunity to comment on the Notice of Proposed Illustrations of Consumer Information on Nontraditional Products (Notice) published by the Office of Comptroller of the Currency (OCC), Treasury; the Board of Governors of the Federal Reserve System (Board); the Federal Deposit Insurance Corporation (FDIC); the Office of Thrift Supervision (OTS), Treasury; and the National Credit Union Administration (NCUA) (the regulators).

MBA is submitting this comment letter to OCC on behalf of all the regulators named above in light of the Notice's direction that the agencies will jointly review all comments and that commenters need not send comments or copies to all of the agencies.

MBA appreciates the efforts of the regulators in developing the Guidance on Nontraditional Mortgage Product Risks (the Guidance),[2] in light of increased consumer demand for these products, and in developing the Proposed Illustrations of Consumer Information on Nontraditional Products (Illustrations) to assist regulated institutions in implementing the Guidance. MBA looks forward to working with the regulators to assist in the development of the Illustrations and to otherwise implement the Guidance.

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 500,000 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 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 3,000 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.

[2] 71 Federal Register 58609 (October 4, 2006).

Before offering comments on the Illustrations, the following background section describes the relevant provisions of the Guidance and summarizes the Illustrations to provide context for MBA's comments.

Background

The Guidance published by the regulators on October 4, 2006 sets forth underwriting, risk management and consumer protection concerns to be addressed by federally regulated financial institutions that offer nontraditional mortgage products. The preamble to the Guidance provides that, in general, the Guidance applies to all residential mortgage loan products that allow borrowers to defer repayment of principal or interest. This includes all interest-only (IO) mortgage products and payment option ARMs. It does not apply to reverse mortgages, home equity lines of credit (HELOCs)--other than as discussed in the Second-Liens section of the Guidance--or fully amortizing residential mortgage loan products.[3]

The consumer protection portion of the Guidance asks that communications with consumers, including advertisements, oral statements, promotional materials, and monthly statements, provide "clear and balanced information about the relative benefits and risks of [nontraditional] products, including the risks of payment shock and the risks of negative amortization." [4] The Guidance also asks that institutions provide consumers with information at a time that will help consumers select products and choose among payment options. It provides that institutions should offer clear and balanced product descriptions when a consumer is shopping for a mortgage--such as when a consumer makes an inquiry to the institution about a mortgage product and receives information about nontraditional mortgage products, or when marketing relating to nontraditional mortgage products is provided by the institution to the consumer--not just upon the submission of an application or at consummation. The provision of such information is intended to supplement the disclosures currently required under the Truth in Lending Act (TILA) and its implementing rules, Regulation Z.

In order to implement the Guidance, the Notice proposes three Illustrations for comment:

- Illustration 1 entitled "Key Facts About Interest-Only and Payment Option Mortgages" briefly describes interest-only and payment option mortgages and provides information on home equity, prepayment penalties and no doc/low doc mortgage loans.

- Illustration 2 entitled a "Comparison of Sample Mortgage Features" is a chart comparing how much borrowers pay under several $180,000, 30-year mortgage loan products. The chart compares amounts under a fixed rate mortgage paying

[3] Ibid, p.58613, footnote 1.
[4] Ibid, p. 58617

principal and interest to amounts under such a mortgage paying interest-only to payments under a 5/1 ARM, an interest-only ARM and a payment option mortgage. The chart shows for each of these products, monthly payments for years one through five, year six with no change in interest rates, year six with a two percent rise in rates, and year eight with a five percent rise in rates. The chart also shows how much a borrower will owe under each product after five years and whether the borrower will have reduced the mortgage loan balance after five years of payments and, if so, by how much.

- Illustration 3, designed to be provided if institutions provide monthly statements for payment option mortgages, details the amounts of principal and interest, interest-only and minimum payments and their respective implications for the borrower's mortgage loan balance.

The Notice indicates that the Illustrations are not intended to be model forms and institutions are not required to use them. Instead, they are provided to show the type of information that the Guidance contemplates.

The Notice specifically invites comment on all aspects of the Illustrations including whether the Illustrations, as proposed, would be useful to institutions, including community banks, seeking to implement the "Communications with Consumers" portion of the Guidance, whether the Illustrations as proposed would be useful in promoting consumer understanding of the risks and material terms of nontraditional mortgage products, as described in the Guidance, or whether changes should be made to them. Finally, comment is sought on whether there are other illustrations relating to nontraditional mortgages that would be useful to institutions and consumers.

General Comments

Disclosures Need to Be Improved Comprehensively. MBA's comments on the Proposed Guidance strongly urged that the regulators use the existing authorities under the Truth in Lending Act (TILA) to improve disclosures for nontraditional products nationwide. Notwithstanding that the OCC and the other regulators determined that new information as set forth in the Guidance was needed now, to ensure that consumers get the information they need about nontraditional mortgages, MBA urges that the regulators should regard the new disclosure Illustrations as a temporary approach. MBA recommends that the regulators direct their energies toward a much more comprehensive approach to improving the mortgage disclosure process for consumers and make these disclosures applicable to all mortgage lenders.

Consumers today confront a pile of disclosures when they apply for and close on a mortgage. Sadly, every new layer of disclosure simply increases the likelihood that the consumer will merely initial all of them without even a cursory reading. For this reason, disclosures do not need to be added; they need to be combined, streamlined and made much more user friendly.

Efforts at improvement should include all disclosures required by Federal law. Because the Real Estate Settlement Procedures Act (RESPA) and TILA apply to regulated and unregulated entities, such an approach is the best means of assuring that virtually all consumers receive high quality information and that a level playing field of disclosure requirements is established for all industry originators. These efforts should also consider the plethora of state disclosures.

Generic Information Can Be Provided to Consumers Earlier in the Process but More Detailed Information Should Accompany the GFE and Any Early TILA Disclosures. The Guidance states that institutions should provide consumers with information at a time that will help consumers select products and choose among payment options.

MBA believes that borrower education, to help consumers navigate the home buying and mortgage finance process, is extremely important and should come as early as possible, before a borrower shops for a home and enters the mortgage process. Effective education aids consumer understanding of key credit terms and differences in the costs and use of various types of products. However, the provision of certain disclosures too early in the process presents challenges for the industry and concerns for consumers.

MBA urges that the final Illustrations should make clear that consistent with the Guidance, Illustration 1 could be provided as early as possible to consumers – by lenders as well as other service providers – when they are shopping for a mortgage, and that Illustration 2 should be provided along with mortgage loan specific disclosures required under TILA and RESPA. Even if Illustration 2 contains hypothetical numbers, there is real danger that it may give the borrower the misimpression that such numbers may pertain when the borrower applies for a mortgage loan. For this reason, Illustration 2 should be provided to the borrower at time of application, in accordance with the time frames for RESPA and TILA disclosures. The borrower may consider this disclosure more effectively at that time in choosing among mortgage products when he or she is also armed with information on closing costs and the costs of credit.

Care Should Be Taken to Assure that the New Illustrations Are Consistent with the Pending CHARM Booklet. The Federal Reserve is currently revising the Consumer Handbook on Adjustable Rate Mortgages (the CHARM Booklet) and provided MBA and other organizations an opportunity to submit comments. Recently, the Federal Reserve issued a new booklet entitled “Interest-only Mortgage Payments and Payment-Option ARMs—Are They for You?” MBA believes that all of these issuances should be carefully scrutinized to assure that they are consistent with each other. Moreover, they should also be revised to provide balanced information on the benefits as well as the risks of nontraditional products. Other borrowers, originators and service providers, including real estate agents, will describe these benefits; these booklets should as well.

The Illustrations Themselves Should Be More Balanced and Provide Information on the Benefits of Nontraditional Products, Too. Notwithstanding the Guidance's direction that consumer information be "clear and balanced," and provide both the risks and benefits of products, neither Illustrations 1 or 2 include such benefits. MBA strongly urges that such benefits be included and MBA offers specific suggestions for this purpose in the specific comments on the Illustrations below.

The Illustrations are Useful but Changes Should be Made to Them. MBA supports the regulators' position that that the Illustrations should not be considered model forms thereby permitting institutions to elect whether to use them. Nevertheless, because many institutions will use the model forms as a guide, we suggest that the Illustrations be revised in accordance with the following comments.

Specific Comments

Illustration 1

The description of interest-only mortgages fails to include any discussion of the benefits of these products. Accordingly, in the interest of providing a balanced presentation, the material should be revised to point out that an interest-only mortgage allows a borrower to make considerably lower payments during the interest-only period. The text should also explain that many borrowers choose this product if they plan to move or refinance before the interest-only period is over. The text could also state that if the amount borrowed exceeds the value of the property because of a decline in real estate prices, refinancing without additional borrower contribution of funds will be more difficult and more costly.

Also in the interest of balance, the description of payment option mortgages should include a statement of the benefits of the product, e.g., that borrowers choose it if they wish to have the flexibility to decide among the various options--recognizing the ramifications of consistently making the minimum payment. The text should also note that many borrowers whose income fluctuates over the course of the year benefit from this product.

In the paragraph entitled "Home Equity," in the interest of clarity, the penultimate sentence should read "This may make it harder to refinance your mortgage, or lessen the amount of funds you receive from the sale of your home."

Also in the interest of clarity, in the paragraph entitled “Prepayment Penalties,” the third sentence should read: “Ask whether your mortgage has a prepayment penalty and, if so, how much it will be and how long it applies.”

Illustration 2

MBA supports the point in the Proposed Illustration that institutions seeking to follow the recommendations set forth in the Guidance could: elect to use or not use the Illustrations; provide information based on the Illustrations; or expand, abbreviate, or otherwise tailor any information in the Illustrations as appropriate to reflect, for example, the institution’s product offerings. These changes could include deleting information about mortgage loan products and loan terms not offered by the institution, revising the Illustrations to reflect specific terms offered by the institution as well the consumer’s particular loan requirements or, based on current market conditions, changing loan amounts and interest rates.

These points should be reiterated in the final Guidance so that each institution can have maximum flexibility to tailor the illustration to their product mix and market. Moreover, since some institutions offer only interest-only mortgages and not payment option mortgages and vice versa, we would strongly urge that separate Illustrations be developed to compare IO mortgages to fixed rate mortgages and to compare payment option mortgages to fixed rate mortgages.

The amounts in Illustration 2 assume that the borrower will make only the minimum required payment. The Illustration should make clear, however, that the consumer can choose to pay more than that. In this vein, the last two rows concerning how much will be owed after five years and what the change in the balance should say that these amounts are based on only the minimum payments. Providing an example based upon the fully indexed, amortizing payment would be closer to what the Guidance seeks.

Finally, in the interest of providing clear and balanced information, we would suggest that the chart should include a field to provide the borrower information on “How Much You Will Pay over 5 Years” after the field concerning how much the borrower will owe. Such a field would highlight the benefit of option ARM and IO products and would be helpful to those borrowers who seek to minimize costs in the interest of affordability. It would also be worthwhile to note that borrowers tend to move or refinance within five years.

Illustration 3

Although the Guidance asked that monthly statements on payment option ARMs provide information to help consumers make informed payment choices, including an explanation of each payment option available and the impact of that choice on mortgage loan balances, MBA is concerned that monthly statements may not always be the best vehicle for reminding consumers of the consequences of mortgage loan choices.

Monthly statements, as routine documents, might not get the borrower's attention to the same extent as a separate mailing. For this reason, MBA would strongly suggest that in the final Illustrations and in implementing the Guidance, institutions, at their discretion, be permitted flexibility to provide borrowers other separate notices, quarterly or otherwise, in lieu of notices in monthly statements to call borrowers' attention to the impact of their payment option choices.

Also, some lenders do not currently have the automated systems to provide monthly minimum or interest-only payment amounts in each monthly statement. MBA believes that, to the extent the monthly statement form is called for, it should be sufficient for the form to provide the borrower with the impacts of each type of payment, without necessarily including payment amounts. The instructions accompanying Illustration 3 should be revised accordingly. The form for example could advise that: "If you make only the minimum payment due, your payment will not cover the interest on your loan and your loan balance will increase. You can avoid an increase in your loan balance by making a payment covering all of the interest on your loan for this month as shown [identify where on the statement the amount of interest for the month is stated]. You may also choose to make a larger payment of principal and interest that will reduce the principal balance of the loan."

If, however, specific payment information is to be called for on a monthly basis, then sufficient implementation time must be provided to allow lenders to make necessary systems changes.

CONCLUSION

Again, MBA greatly appreciates the opportunity to comment on these Illustrations. The availability of the widest possible range of products that will serve consumers' financing needs and ensure they receive useful information on such products are matters of critical importance to MBA. MBA looks forward to continuing to work with the regulators on these issues.

For further information concerning these comments, please do not hesitate to contact Ken Markison at kmarkison@mortgagebankers.org and (202) 557-2930 or Corey Carlisle at ccarlisle@mortgagebankers.org and (202) 557-2860.

Most sincerely,

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