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April 20, 2004

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Robert E. Feldman, Executive Secretary
Attention: Comments
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Ms. Jennifer J. Johnson, Secretary
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Washington, DC 20551
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Regulation Comments
Chief Counsel's Office
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1700 G Street, NW
Washington, DC 20552
regs.comments@ots.treas.gov

Re: **FDIC** 12 CRF Chap. III; **FRB** Docket No. R–1180; **OCC** Docket No. 004–05: **OTS** Docket No. 2003–67; Agency Compliance with Section 2222 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996; 69 Federal Register 2852; January 21, 2004

Ladies and Gentlemen:

Section 2222 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA) requires federal banking agencies (Agencies) to review their regulations at least once every 10 years. The Agencies are now in the second phase of this review and are asking for comments from bankers on the ways in which the Consumer Protection: Lending-Related Rules may be outdated, unnecessary, or unduly burdensome. The American Bankers Association (ABA) brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership - which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks - makes ABA the largest banking trade association in the country.

While preparing this comment letter and our previous comment letter in the first phase on specific regulations, ABA has detected some overarching concerns about the regulatory process and the overall level of burden. We are working with several of our banker committees on developing comments on the process that do not exactly fit under a particular regulation.

First, our bankers are concerned that not only do the Agencies not always consider the overall bank regulatory burden in making new regulatory proposals but also they and other regulators do not always take into account regulatory burden arising from those other regulators. For example, the Department of Housing and Urban Affairs recently proposed a revision of Regulation X implementing the Real Estate Settlement Procedures Act that was inconsistent with existing Truth in Lending Act regulations, and which, if adopted, would have created much new burden. Thus, we believe that it is not enough just to review banking regulations. The Agencies and the industry need to review the entire burden of regulation on banking.

Second, bankers are expressing concern that some regulatory proposals from the Agencies suggest that the staff members writing the proposals are not as familiar with banking practice and the current level of regulatory burden as they might need to be. For example, ABA believes that it is crucial to reducing the regulatory burden to minimize changes to existing regulations as much as possible and to avoid new regulations. As one banker put it, "Just hold still!" ABA is concerned that the cost and burden of regulatory changes and new requirements are often underestimated. It is assumed that a new disclosure or revision to an existing disclosure means simply purchasing the correct new forms and software. But if usually involves much more. Banks must monitor for changes to existing regulations and new requirements, review them, make necessary modifications, order new forms and programs, revise websites and advertisements, educate staff, prepare staff for customer inquiries, and implement auditing measures.

Too frequently, Congress adopts new requirements without weighing the costs and benefits. Our Agencies should send the message to Congress that it should be more sensitive to regulatory burdens when adopting new statutory requirements. The Agencies' input during the legislative process would also be helpful. The Agencies also could be more sensitive to regulatory burdens and costs when proposing changes to regulations. A good example is the Federal Reserve Board's (Board) proposal in late 2003 to alter the meaning of "clear and conspicuous" for virtually all required consumer protection disclosures. While well intentioned, the Board's staff seemed unaware that all forms, all documents, all software programs, all advertisements, websites, education materials, etc. would have to be reviewed, revised, and redistributed and that staff would have to be reeducated. The Board's staff also seemed to equally underestimate the costs associated with potential litigation, both the actual costs as well as the costs associated with litigation avoidance, all well-documented costs. And yet, there is little if any evidence that the existing disclosures are inadequate so as to justify these enormous new compliance costs.

Third, review of the utility of the Paperwork Reduction Act suggests that it is not effective in reducing or preventing additional paperwork. This is partly because of the statutory change in 1995 that allowed additional paperwork burden to be added, even though the public had demonstrated that the actual burden estimate was seriously incorrect.

Fourth, actually estimating the cost of the regulatory burden is extremely difficult and itself is burdensome. Nonetheless, ABA is considering whether some specific regulatory cost and burden surveys or studies might not be needed as part of this EGRPRA process. These overarching concerns need to be addressed separately from just a burden review of individual regulations, and ABA will be providing separate comments on these issues.

Comments on the Consumer Protection Regulations Relating to Lending

ABA makes the following recommendations under the Agencies' request for comments. As noted above, some of these regulations have already been reviewed and extensively revised within the last five years, such as Regulation M, Consumer Leasing, resulting in significant reduction in regulatory burden, and we did not receive any suggestions for improvements from our bankers.

1. Fair Housing

Proposed Regulatory Changes
In 1997, as part of a regulatory burden review under Section 303 of Reigle Community Development and Regulatory Improvement Act, the Federal Deposit Insurance Corporation (FDIC) amended its fair housing regulations to make them conform to the requirements of the Board's Regulations B and C. In doing so, the FDIC eliminated additional recordkeeping for small institutions not covered by the Home Mortgage Disclosure Act (HMDA). However the Office of the Comptroller of the Currency (OCC) still has requirements for additional recordkeeping for institutions not covered by HMDA, although the OCC exempts institutions from this recordkeeping if they have less than 50 reportable mortgage applications per year. Neither the Office of Thrift Supervision (OTS) nor the Board appear to have any additional fair housing recordkeeping requirements above those required by Regulations B and C. ABA recommends that the OCC eliminate its additional fair housing recordkeeping requirements and reduce its regulatory burden to conform to the other agencies and the requirements of Regulations B and C. ABA also recommends that both the OCC and OTS eliminate their requirement (not found in Regulation C) that the reasons for denial be recorded.

Proposed Legislative Changes
None.

Proposed Administrative Changes
See discussion under Regulation B.

2. Loans in Identified Flood Hazard Areas

Proposed Regulatory Changes
None.

Proposed Legislative Changes
1. The mortgage market has changed appreciably since the advent of the National Flood Insurance Program through passage of the National Flood Insurance Act of 1968 and its subsequent revisions. The 1968 Act established the framework for addressing the financial, personal and community losses engendered by floods. Financial institutions became the key to such a system by requiring that banks not "make, increase, extend or renew" any loan unless commercial or residential buildings securing the loan are covered by flood insurance. Thus, the flood insurance program has no real teeth unless buildings are used as security on loans. All other buildings are effectively excluded from

the program. Banks are the enforcers of a national policy and are subject to compliance risks not evenly distributed throughout the country.

Federally insured financial institutions and their subsidiaries no longer make the lion's share of mortgage loans. Nor do they generally hold the loans any longer until they are paid off. Large mortgage banks and mortgage brokers, not supervised by the Agencies, originate a substantial portion of the loans in today's market. In addition, a considerable number of loans being serviced in today's environment are serviced by independent service operations or by servicers that are affiliated with holding companies. These institutions are not necessarily subject to supervision or regulation by the Agencies. In addition to the changes in the mortgage market, significant portions of properties in special flood hazard areas (SFHA) are not covered by flood insurance regulations, since they are either owned without a loan from a supervised financial institution or financed through institutions not covered by the regulations.

From a public policy perspective, should the purpose of the Flood Insurance Program be just to protect banks from losses on federally-related mortgages or should it be to ensure that communities damaged in floods will be able to rebuild? We believe the public interest is better served by adoption of the latter purpose. A more effective approach today might be to require that federal flood insurance policies be issued through the various city and county governments as a component of regular property assessments and taxes. The Federal Emergency Management Agency has a significant working relationship with these governments throughout the country. It could develop a program for these governments that would mirror the existing Write Your Own program that it utilizes with selected insurance companies. In this manner all properties within a designated special flood hazard area could be covered not just those whose owners obtain a loan from a regulated financial institution. Actuarial rates and loss mitigation efforts could be more realistically established.

Establishment of such an approach would remove a substantial expense currently embedded in the mortgage lending and servicing process. Collection of premiums would be standardized throughout the regular property assessment system. The current disclosure requirements, determinations of whether properties are or will be located in a SFHA, obtaining and maintaining insurance, etc. and the compliance risks imposed by these requirements would no longer have to be imposed on the financial institutions.

2. An additional issue is the amount of coverage, particularly when financial institutions must force-place insurance. Most consumers do not understand that flood insurance will only cover the mortgage amount, not the replacement value. If total loss occurs, the bank is made whole but the owner is left without anything with which to rebuild. Again, besides being confusing to most customers, this approach is not consistent with a public policy to provide insurance for a community to recover from a disastrous flood. Also, customers would better understand their flood insurance policies if the policies more closely track the replacement value format of their hazard insurance policies.

3. Several of our agricultural lenders report difficulties on agricultural real estate lending. The statute clearly states that there are to be no exceptions for agricultural real estate. However, these bankers report that this inflexibility creates situations where the intent of the statute (protecting the collateral security of regulated institutions against flood risk) is not serving its intended purpose. For example, the agricultural lender may take a mortgage over a parcel of agricultural land covering hundreds of acres and advance 65% against the appraised value. However, the land may have a barn

or machinery shed (a "walled and roofed structure") that has no impact on the income-producing capacity of the land and provides little material value to the collateral. In many cases, the "walled and roofed" structures may not even be used in the farming operations because they are old and obsolete. However, if these structures are located in a flood zone, then the bank must require that the borrower purchase flood insurance. In reality, the bank may have a mortgage on agricultural land of $1 million with a loan value of $650,000 but the regulations still require that the borrower purchase flood insurance for a shed with a cash value of $10,000 (1% of the total collateral value). In reality, the flood insurance does not provide any meaningful value to the bank and potentially creates ill will against the bank when the borrower is forced to pay for it. The statute should permit an exception for agricultural real estate where the bulk of the collateral is represented by land. Perhaps a bank could be permitted to set its own policy for flood insurance, when the value of the permanent structures on agricultural real estate does not represent a meaningful percentage of overall collateral value, such as less than 10% of the total value, and the bank's advance rate does not exceed 75% (excluding the value of the structures).

The requirement for life of loan monitoring also creates burdens for a bank that finances agricultural real estate. Using the example noted above, if a borrower decides after loan funding to build a tractor shed on his land and that shed is in a flood zone, then the bank must require the borrower to purchase flood insurance (and even force place it, if necessary). However, the value of the shed may be meaningless as a percentage of the overall collateral value of the land.

The statute is not clear when discussing acceptable deductibles or even how much to value the permanent structures. For example, the statute implies that if a building has a value less than the deductible of a policy, then flood insurance is not required. However, if the bank decides that a credit-worthy borrower merits a higher deductible on flood insurance, it is unclear if it may then waive the requirement for flood insurance if the building has a lesser value. Also, many appraisers assign no market value to a farm building (in fact, it may detract from overall land value). Further, the statute is unclear if this situation permits the bank to waive flood insurance.

4. Finally, when a flood policy lapses after 30 days, a financial institution is required to force-place flood insurance to protect its loan, but only after 45 days. Thus the law appears to require that the financial institutional be exposed to total loss in case of flood for at least two weeks. This makes no sense, and needs to be corrected to allow forced placement BEFORE insurance coverage lapses.

<u>Proposed Administrative Changes</u>
Our bankers tell us that obtaining current flood maps and flood location determinations continues to be a difficult task. The Federal Emergency Management Agency should ensure that the process of updating flood maps is a priority project.

3. Consumer Leasing (Regulation M)

<u>Proposed Regulatory Changes</u>
This regulation was reviewed and revised in 2001, and ABA received no suggestions for changes during this current comment period. However, we received a number of requests that the Board not adopt any changes to the existing requirement for "clear and conspicuous" disclosures for this regulation. See ABA's letters to the Board on Docket Nos. R-1167 through R-1171, dated February 2, 2004, and March 23, 2004 (from ABA's Compliance Executive Committee).

Proposed Legislative Changes
None.

Proposed Administrative Changes
None.

4. Equal Credit Opportunity (Regulation B)

Proposed Regulatory Changes
A recent issue with the March 2003 amendments to Regulation B and its Commentary involving joint applications provides another example of how regulatory changes, which appear to be minor, can create confusion and compliance burdens. The Board modified the regulation to clarify the need for creditors to document that co-applicants have applied for a loan. The Board also added language to the model forms so that applicants could specifically indicate whether they were applying jointly or individually.

While the Board stated that written applications are not necessary (except where otherwise required) and that model forms are optional, some institutions and examiners concluded that the changes required written applications and that the language added to the model forms is mandatory. They reason that the Board would not have altered the model forms unless the new language was mandatory. On this basis, some creditors altered their forms. Further, bankers remain confused as to whether certain secondary market forms are in compliance with the regulation. While the Board has indicated that they are, another regulator's examiners have been telling bankers that they are not. Several bankers have told us that their examiners are now interpreting the change as requiring a new and separate document that positively affirms all applicants intend to apply for credit.

To avoid unnecessary revisions to documents and procedures, the Board should keep in mind that changes to model forms may be viewed as mandatory or "preferred," as compliance officers see risks in not adopting officially sanctioned forms or language, notwithstanding the advisory that they are optional. Retaining current forms along with new language would reinforce the concept of flexibility and choice. In addition, the Board should work with other bank regulators so that all agencies and their examiners are interpreting the regulations consistently.

Proposed Legislative Changes
None.

Proposed Administrative Changes
A number of bankers have been troubled by the lack of guidance provided by the Agencies on fair lending, arising under either the Fair Housing Act or the Equal Credit Opportunity Act. Bankers were aided by the joint interagency guidance issued on fair lending in 1994. However, the ten agencies involved in issuing that guidance stated at the time that they anticipated releasing additional guidance, but a decade has passed without such. Meanwhile, there have been only a few settlements of fair lending violations in that time, and bankers uniformly find the wording of these settlements to be so vague and general that it is impossible to glean very much, if any, compliance guidance from them. For example, in the written agreement by the Board with a state member bank settling violations of discrimination in lending in 1999, it is impossible to determine the nature of the violations, whether they involved direct and/or indirect lending, whether they were inadvertent or intentional, or almost anything else that might instruct bankers on compliance with fair lending laws.

Department of Justice settlements generally are equally vague. While parties to a written agreement or a settlement might actively negotiate for such lack of specifics, we urge the Agencies to provide more guidance, even if couched in various hypothetical examples, rather than continuing to leave bankers in the dark about developments in fair lending enforcement.

5. Home Mortgage Disclosure Act (Regulation C)

Proposed Regulatory Changes

1. It is impossible to estimate the added burden from the revised HMDA data collection issued by the Board in 2002, but it is enormous. None of our bankers thought it realistic just to ask for it to be rolled back. However, one item in the revision has caused significant problems and at the same time seems to add more noise than value to the system: the revised definition of "refinancing." In an effort to simplify and make more consistent reporting of refinancings, the Board adopted a new definition that is very easy to apply: if a loan obligation is refinanced, and the original loan was secured by residential property and the new loan is secured by residential property, there is a reportable refinancing. Our bankers find this new definition is too broad, creates great burden, and distorts the data. The primary problem is the numerous small business loans on which a mortgage on the business owner's house has been taken, usually "out of an abundance of caution" and therefore not reportable when it is originated. However, a refinancing of this small business loan is now HMDA reportable. A number of bankers have indicated that up to half or even 60% of their small business loan refinancings, which are often done on an annual review and refinancing basis, are now to be reported as HMDA loan refinances. As many of these loans are for $1 million or more and are located in business areas, these bankers believe that the HMDA aggregate reports for their institutions will be markedly different for 2004 public data compared with their 2003 public data. As these loans are not home mortgage loans in any normal sense, our bankers believe that this new reporting will greatly skew the 2004 HMDA data. Additional burden is created for our banks' compliance officers, because most of these loans are done in the commercial lending side of the bank, and the commercial lenders have little knowledge or experience with HMDA data collection or reporting, so that training expense and time to collect this new data has been very high. ABA and a number of bankers have already raised this issue with the Board as early as the middle of 2003, but no clear response to this problem has been issued by the Board.

2. A compliance officer has written to ABA pointing out that Code of Federal Regulations (CFR), as published by the Government Printing Office, defines a home improvement loan in Regulation C as:

"(g) Home improvement loan means:
(1) A loan secured by a lien on a dwelling that is for the purpose, in whole or in part, of repairing, rehabilitating, remodeling, or improving a dwelling or the real property on which it is located; and
(2) **A non-dwelling secured loan** that is for the purpose, in whole or in part, of repairing, rehabilitating, remodeling, or improving a dwelling or the real property on which it is located, and that is classified by the financial institution as a home improvement loan."

The banker and at least one compliance training company read this as not covering an unsecured loan. However, the Federal Reserve Regulatory Service reads: **"non-dwelling-secured loan,"** which would cover an unsecured loan. There appears to be some confusion in the legal sources themselves. If the Board means to include unsecured loans, then a technical amendment or correction of the CFR appears necessary.

Proposed Legislative Changes

The Home Mortgage Disclosure Act currently exempts institutions not in an MSA from reporting, as well as very small institutions (under $33 million for 2004 reporting). For nondepository mortgage lending institutions, one of the criteria for coverage is whether the instititution originated 100 or more home mortgage loans. Due to the expense and effort necessary to implement a HMDA reporting system, particularly after the recent revisions greatly increased the reporting burden, ABA recommends that the statute be amended to provide an exemption from HMDA reporting for depository institutions that do not originate 100 or more home mortgage loans.

Proposed Administrative Changes

1. Every year when the Board releases its HMDA data, the industry is subjected to a number of spurious "studies" of the HMDA data to "identify" lenders that are illegally discriminating, despite the fact that the HMDA does not contain sufficient data to make that determination. Additionally, hundreds of media articles appear suggesting that the disparities in denial or in applications are proof of illegal discrimination. ABA believes that regulators need to be more aggressive in refuting such articles and "studies" as invalid, uninformed and harmful to consumers, particularly minority consumers, who are led to believe that they will be discriminated against if they go to a bank for a home loan. Since banks and savings associations are the only institutions that have their loan files actually regularly examined for any evidence of discrimination, this result is the exact opposite of what is needed. If nothing else, the Board should prepare a simple, plain English media guide to what the HMDA data means and how it can be used and misused. Reporters need it.

2. Because of the change in the definition of refinancing, many banks are reporting a number of small business loans as HMDA loans, as discussed above under Proposed Regulatory Changes. There is considerable confusion in the industry as to whether these loans will also be reported as CRA Small Business loans or whether having been reported as HMDA loans they are no longer reportable as CRA loans. Written clarification is needed on this reporting issue.

3. As noted in the general discussion of regulatory burden, bankers are concerned that regulatory changes are not being made on any sensible cost/benefit analysis, nor are compliance deadlines being accurately estimated. The recent HMDA revision is a good example. These changes were so extensive and the systems and training required to be changed or created so complex that bankers had to plead for an additional year to make all of the changes required. While the Board did listen and decide that such a delay was merited, there was some feeling by bankers that the staff simply should have known how difficult it would be to implement these changes and should have never thought that it could have been done by the industry in just six months.

6. Truth in Lending (Regulation Z)

Proposed Regulatory Changes

None.

Proposed Legislative Changes

The provisions of the Truth in Lending Act creating the right of rescission continue to be a problem that add compliance burdens and delay release of loan funds subject to the provisions. Bank

customers have difficulty understanding why they must wait for the funds when refinancing a mortgage or obtaining a home equity loan. From the bank's perspective, the right of rescission is an unnecessary requirement that creates unwanted forms, adds to the settlement paper pile, and lengthens settlement time. Over the last decade, we have only been able to identify one banker who ever recalls a customer exercising the right of rescission within the three-day period, and the case involved a divorce. Banks assert that the right of rescission is only used, or rather misused, in the event of a loan default as a means to avoid repaying the loan or voiding the security interest. The Board should recommend to Congress that it consider exempting regularly examined institutions from this provision.

Proposed Administrative Changes
None.

7. FRB's Unfair or Deceptive Acts or Practices (Regulation AA) and OTS' Unfair or Deceptive Acts or Practices (12 CFR Part 535)

Proposed Regulatory Changes
None.

Proposed Legislative Changes
Our bankers continue to be concerned about "the uneven playing field" in compliance between depository institutions and other lenders. Essentially, bankers know that their loans will be examined for consumer compliance at least once every two years. They also know that nonbank lenders will not have their loans examined, probably ever, because the Federal Trade Commission and the state agencies that have jurisdiction over them do not have the examination and supervision infrastructure to do so. The solution is not to end consumer compliance examination for banks, but it is to fund, by assessment of the nonbank lenders, if necessary, a real supervisory examination program to stop some of the consumer abuse and predatory lending that we hear about constantly. ABA urges the Agencies and the FTC to develop a legislative proposal to actually enforce the consumer protection laws currently in effect against nonbank lenders.

Proposed Administrative Changes
The Agencies have released additional guidance on unfair and deceptive practices (UDAP), which is helpful to our bankers. However, actual enforcement will provide additional guidance. As we noted under Regulation B, there is an opportunity in settlements and written agreements to provide additional guidance to bankers, but it is an opportunity often missed. If the Agencies pursue UDAP enforcement actions, information about them needs to be disseminated to the industry.

Conclusion

As we wrote in our first letter, we note considerable doubt on the part of bankers that this exercise in regulatory burden reduction will be any more effective than the last five or six. Several compliance officers all said the same thing when asked for suggestions for burden reduction: they were too busy trying to comply with the existing burden to try to find ways it might be reduced. We

hope for a real reduction in the regulatory burden under the Community Reinvestment Act, to spark some enthusiasm for this current effort. If there are any questions about this comment, please call the undersigned.

Sincerely,

Paul Smith
Senior Counsel