CONSUMER MORTGAGE COALITION

May 10, 2004

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Home Mortgage Disclosure Act: Revised Formats for Public Disclosure of Lending Data
Docket No. R-1186, 69 Fed. Reg. 15469 (Mar. 25, 2004)

Dear Ms. Johnson:

The Consumer Mortgage Coalition (the "CMC"), a trade association of national residential mortgage lenders, servicers, and service providers appreciates the opportunity to submit its views concerning the proposal ("Proposal") of the Board of Governors of the Federal Reserve System ("Board") to change the way that data collected from financial institutions under the Home Mortgage Disclosure Act ("HMDA") is reported to the public. The Board is proposing to revise its reporting formats to reflect the recent changes in reporting requirements for financial institutions, including changes in race and ethnicity categories and new items such as the rate spread between the annual percentage rate ("APR") on the loan and comparable Treasury rates, for certain higher-cost loans.

The CMC recognizes that the Board's public disclosures must be changed to reflect the changes in the information reported by financial institutions as of January 1, 2004, and, therefore, generally supports the Proposal. But we are concerned that the proposed treatment of pricing information would present an incomplete and potentially misleading picture of a financial institution's lending practices. In view of the difficulties of presenting pricing information in a meaningful way, the Board should consider delaying implementing new reports that include pricing information at least until it has received and analyzed the first year's data.

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Pricing Information

If pricing information is included in the 2004 HMDA reports, it should be done in a way that avoids, as much as possible, compounding the distortion inherent in the HMDA reporting system. The fundamental problem with HMDA reporting has always been that the information reported, such as race and ethnicity and property location, does not reveal legitimate reasons for disparities in acceptance rates and lending patterns, including creditworthiness, debt-to-income ratio, loan-to-value ratio, and the consumer's choice of loan product. Reporting of pricing information, in particular, has the potential to add to this problem because of the unjustified weight that is often attached to a reported statistic, particularly when the source of the number is the federal government. In fact, there is simply no logical connection between the data reported under HMDA and predatory or discriminatory lending. Although this basic problem cannot be cured by changes in the reporting format, we believe that each table should include a disclaimer at the beginning indicating that a loan is not illegal or predatory simply because it is a reportable loan. The disclaimer should also state that APR spread-reportable loans are not necessarily "nonprime" loans. That is, a loan to a borrower may carry a relatively high APR even if the borrower does not have the characteristics often associated in the public mind with nonprime lending, such as a history of financial problems. The APR spread can be reportable because the loan is for a small amount, the loan-to-value ratio is high, the borrower has requested a limited-documentation loan, or for a variety of other reasons.

In addition, we would recommend that the Board avoid using terminology such as "subprime" or "nonprime" in table captions or elsewhere to describe loans on which the APR spread is reportable. As the Board has recognized:

> There is limited public information on the range of prices (particularly APRs) of closed loans in the mortgage market, and there is no absolute demarcation between subprime and prime mortgage markets.

Board of Governors of the Federal Reserve System, Home Mortgage Disclosure; Final and Proposed Rule, 69 Fed. Reg. 7221, 7229 (Feb. 15, 2002). *See also* Board of Governors of the Federal Reserve System, Home Mortgage Disclosure—Final Rule and Staff Interpretation, 69 Fed. Reg. 43218, 43220 (June 27, 2002) (noting that designation of loans as FHA/VA or manufactured home loans in reports will allow "data users" to correct for possible "misclassif[ication]" of those types of loans). Given these acknowledged limitations in the data, it would be inappropriate for the rate-spread-reporting cutoffs to become a *de facto* federal definition of subprime or nonprime lending, which could easily happen if captions, statements by Board staff, or information accompanying the release of HMDA date described these loans as "subprime" or "nonprime." References that might be considered pejorative, such as "high-cost loans," should also be avoided. The Board should instead use a neutral term such as "rate-reportable" loans.

The pricing data for 2004 will be particularly problematic because the spreads on many loans will not be reportable under the transition rules issued by the Board. For that reason, the CMC believes that the Board should delay any decision as to how pricing information should be reported until next year. Delaying the decision will also allow the Board to fine-tune its reports after receiving and analyzing the first year's data.

If the Board decides to report pricing information beginning with 2004 data, it should minimize the potential for distortion by (1) including all of an institution's lending activity in its reports and not arbitrarily excluding government-backed loans; (2) not reporting average prices, which are inherently misleading because pricing is reported only for higher-cost loans; (3) itemizing pricing information by loan amount, which helps explain legitimate reasons for pricing disparities; and (4) reporting rate-spread information and HOEPA status for purchasers. The Board should also (5) include a note on each report explaining the potential disparities between reportable HOEPA loans discussed in the preamble, to avoid having the report of HOEPA status create a distorted picture of an institution's lending practices.

1. The Board should include FHA and VA loans in the reported pricing data.

We believe that excluding government-backed loans, as the Board has proposed, will create a seriously distorted picture of many institutions' lending practices. For example, suppose an institution predominantly makes FHA or VA mortgage loans, but also makes a small number of "super-jumbo" loans to very wealthy individuals and has an active outreach program that involves making nonprime loans to credit-impaired borrowers in low-to-moderate income areas. If this institution's FHA and VA lending is excluded, then it could appear that the institution is not serving its community when it actually may be doing a better job than another institution that mostly makes conventional loans and does not have a nonprime lending program.

The Board asserts in the preamble that government loans do not raise questions about pricing. We respectfully disagree. Because of government-imposed upfront charges that increase the APR, a disproportionate number of government-backed loans will be APR-spread reportable, and lenders' practices with respect to government-backed loans have created their share of controversy. Furthermore, excluding a significant portion of many institutions' lending activity is contrary to the Board's goal in collecting rate-spread information of providing a more detailed and sophisticated understanding of lenders' practices. FHA and VA loans are generally priced between prime conventional loans and nonprime loans, so that omitting them can make it look as if an institution is not serving that range of customers.

2. Reports should not include mean and median rate spreads.

Since rate spreads are only reported when the APR is more than three percentage points above the comparable Treasury rate for first-lien loans or five percentage points above the comparable Treasury rate for second-lien loans, the mean and median rate spread provide almost no meaningful information about a lender's actual lending practices. Many, if not most, of a lender's loans would not be included in the calculation because they fall below the cutoff. Therefore, one institution could easily have a higher reported mean and median rate than another, when the first institution's overall average rates were lower and the first institution was doing a better job than the second of serving the needs of low- and moderate-income individuals.

At the same time, these "average" figures create the potential for very misleading media reports, and will likely be cited in any "predatory lending" litigation against an institution, regardless of whether they actually reflect unfair or discriminatory practices. Reporting this information could actually create a perverse incentive for some institutions to *raise* the APR on some loans that are now slightly below the reporting cutoff, so as to improve their reported mean and median rate spreads.

3. Any report of pricing should include the loan amount.

Nonprime lending entails significant fixed costs, regardless of loan size. As a result, upfront costs, many of which are reflected in the APR, are higher for low-denomination loans. If the Board decides to report APR spreads in 2005, it should itemize them by loan amount so that the public can better understand at least one legitimate reason for pricing disparities.

4. APR spread and HOEPA status should be itemized by type of purchaser.

Table 3 ("Loans Sold, by Characteristics of Borrower and of Census Tract in Which Property Is Located and by Type of Purchaser") could be modified to include this information or it could be presented in a separate table. The new Table 11 series ("Pricing Information for Conventional Loans on 1-to-4 Family Owner-Occupied Dwellings") will show considerable detail about loan pricing in originated loans. The public should be able to evaluate similarities and differences in pricing between loans that institutions originate and hold, and loans that are later purchased by investors, particularly government-sponsored enterprises ("GSEs"). An analysis of loan pricing by the race, ethnicity, and income of the borrower and the income and demographics of the census tract in which the property is located is not complete without data on the subsequent purchasers of these loans.

Since the GSEs have instituted risk-based pricing programs in order to meet their risk-based pricing goals, pricing and HOEPA-status data should also be included. One simple way to show pricing spreads by purchaser would be to add rows to the bottom of Table 3 that correspond with the pricing-spread columns found in Table 11. Another way to disclose pricing spreads by purchaser would be to replicate the Table-11 series format and produce one such table, consisting of all loans, for each purchaser. The Board should also publish aggregate tables for each of the purchaser codes using the same format.

By accounting for loans sold into the secondary market, information about purchasers would allow a more complete analysis of an institution's pricing patterns. It would also provide more information about the loan pricing policies of the GSEs and other secondary-market purchasers.

5. Reports should explain that the HOEPA loan category might not exactly match the highest APR-spread brackets.

As the Board notes, the highest APR-spread bracket on the proposed disclosures roughly corresponds to the HOEPA loan category, but there are differences because the calculation date differs and HOEPA can be triggered by a "points and fees" test. If there are more HOEPA loans than high-bracket loans, industry critics or the media may conclude, correctly or incorrectly, that the institution is charging excessive up-front fees that are pushing loans into the HOEPA category. Therefore, reports that reflect HOEPA loan status should include a note stating that there may be a variety of reasons for any mismatch between HOEPA loans and loans reported in the highest rate-spread brackets.

<u>Other Issues</u>

As noted, the CMC supports several aspects of the Proposal. In particular:

- We support the Board's approach to the itemization of manufactured home lending data, which is being collected for the first time. The Board is proposing to continue to include manufactured home loans in existing categories, while including a separate column for manufactured homes. This approach will keep reported data for the existing categories consistent with the numbers for those categories in previous years.

- We support the proposal to create a separate reporting category for consumers who identify themselves with more than one minority group. The alternatives would appear to be to introduce the concept of a "fractional" borrower (allocating a portion of each individual's information to each group that was checked on the monitoring form) or to "over-count" such individuals once in each group. Either of these alternatives would be confusing and would reduce the value of the reports. We note that the value of mixed-group statistics will be reduced because of the requirement to code consumers who are identified as white as well as members of more than one minority as members of the minority. We recognize that this reflects a government-wide requirement, but it is still unfortunate because it will distort the statistics.

Finally:

- The CMC does not support the proposals to delete Table 6 and gender information from other tables. The Board notes that this information is relatively unused, but the reason may be that, even given the severe limitations of HMDA data, it is clear to the public that institutions are not discriminating based on sex. As with government-backed loans, it would be inconsistent with the goal of presenting a complete picture of an institution's lending practices not to report gender-related information.

- The Board solicits comment on whether it should include census tract data for Puerto Rico in several reports of lending by racial/ethnic composition of census tracts. We recognize the Board's concern that including this information, when it was previously excluded because of the lack of census data, would make trend analysis more difficult. But we believe it should be included because it better reflects an institution's pattern of lending, particularly to Hispanic customers.

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For the reasons stated, although we generally support the Proposal, we urge the Board to reconsider its proposed method of reporting pricing information and to make other changes. We appreciate the opportunity to present our views.

Sincerely,

Anne C. Canfield
Executive Director