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VIA EMAIL

August 15, 2007

Ms. Jennifer J. Johnson,
Secretary,
Board of Governors of the Federal Reserve System,
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: **Docket No. OP-1288**

Dear. Ms. Johnson:

I am writing from Woodstock Institute to comment on the adequacy of existing regulation protecting consumers in the home mortgage lending market. Woodstock Institute is a Chicago-based nonprofit research and policy organization that for over 33-years has promoted access to affordable and responsible financial services in lower-income and minority communities. Woodstock Institute conducted some of the first research documenting the disproportionate concentration of subprime loans in minority communities. The Institute has also illustrated the relationship between increased levels of subprime loans and skyrocketing foreclosures in minority communities and quantified the impact that foreclosures have on neighborhood property values. Woodstock Institute has worked closely with local, state, and federal policy makers to craft legislation limiting some of the most abusive practices in the subprime industry and worked with regulated financial institutions to promote responsible, prime lending in minority neighborhoods. Woodstock has also provided testimony at previous hearings on the adequacy of the Home Ownership and Equity Protection Act (HOEPA).

We have great concerns about the regulatory response to the current crisis in the subprime mortgage market. For years, regulatory agencies have chosen to allow mortgage loans with extremely risky features and increasingly loose underwriting standards to proliferate the subprime market. From 1999 to 2006, the percent of subprime loans that were 2/28 or 3/27 ARMs went from 53 percent to nearly 77 percent. At the same time, underwriting standards in the subprime market were substantially eroding. In 2000, 23 percent of subprime loans were low doc loans that required limited documentation of borrower income or assets. In 2006, this number increased to nearly 43 percent. Meanwhile, the equity positions of subprime borrowers worsened. In 2000, 35 percent of subprime borrowers had loan-to-value ratios greater than 80 percent. By 2006, this number had increased to nearly 63 percent.

While this was happening, federal regulators took no action. While we support the protections contained in the most recent interagency statement on subprime lending (July 10, 2007), it is critical that these protections cover loans originated by all lenders. The Federal Reserve has the power under HOEPA to approve regulations that protect consumers from loans with unfair and deceptive terms.

We believe that:

Prepayment penalties should be significantly restricted on ARM loans where payments will adjust in three years or less. At the minimum, prepayment penalties should not extend beyond the initial "teaser" period. Borrowers should be given a window of 90-days prior to the end of the teaser period in which they can refinance their loan without incurring a prepayment penalty.

Escrow for taxes and insurance should be required on all mortgage loans. A common practice in the subprime market is for mortgage lenders to obscure the true cost of home ownership by not requiring borrowers to make monthly payments to an escrow account for the purpose of paying property taxes and property insurance. Property taxes and property insurance are required costs of home ownership. All too often, subprime borrowers fall into trouble with their mortgages when hit with their first property tax bills. This problem would be avoided if borrowers were regularly contributing to monthly escrow accounts from which property taxes and insurance would be paid.

Lenders should be required to verify a borrower's income on subprime mortgages. We see no reason why borrower income should not be verified on subprime loans with risky features, such as hybrid ARMs. The opportunity for fraud and abuse on such loans is too great.

Lenders should not conceal the true cost of a loan in order to qualify the borrower for a mortgage the borrower cannot afford. When underwriting subprime loans, lenders must consider all monthly housing related payments. This includes the monthly costs of principal, interest, real estate taxes, and insurance. Lenders should not exclude the costs of taxes and insurance from debt-to-income calculations to artificially keep monthly housing costs down. Borrowers must also be informed of the monthly costs associated with real estate taxes and insurance. For mortgages with a low initial payment, but subsequent higher payments and adjustable rates, lenders should underwrite loans to the fully indexed rate and not the teaser rate in the loan's initial period. Lenders must clearly inform borrowers of the terms of a loan and any feature that may result in payment shock. Borrowers must be made aware of the true cost of any future adjustments in payment, balloon payments, and prepayment penalties.

It is critical that the Federal Reserve Board take action to protect consumers and restore confidence in the mortgage market. Currently, HOEPA is insufficient to protect consumers from the riskiest and most abusive loan terms in the subprime market, and the interagency subprime guidance does not apply to all lenders. At a minimum, the Board must use its rulemaking authority under HOEPA and adopt the above guidelines in order to protect consumers from mortgages with unfair and deceptive terms.

Sincerely,

Geoff Smith
Research Director

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