ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA

Submitted via email -- regs.comments@federalreserve.gov

May 2, 2011

Jennifer J. Johnson, Secretary
Board of Governors of the
Federal Reserve System
20th Street & Constitution Avenue, NW
Washington, DC 20551
Attention: Docket No. R-1406

Re: Proposed Rule Amending Regulation Z (Truth in Lending) to Implement Certain Requirements Regarding Escrow Accounts

Dear Ms. Johnson:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the Federal Reserve's proposed amendments to Regulation Z (Truth in Lending) to implement certain amendments made by the

[1] *The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 20,000 locations nationwide and employing nearly 300,000 Americans, ICBA members hold $1 trillion in assets, $800 billion in deposits, and $700 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)[2] relating to escrow accounts. This proposed rule would require new disclosures for escrow accounts and also provide an exemption for some financial institutions from the escrow requirements for higher-priced mortgage loans.

While ICBA agrees that escrow accounts can be a useful tool for many consumers, we have several concerns with this proposed rule and urge the Federal Reserve to give careful consideration to our comments before implementing final amendments to Regulation Z.

Background

The Federal Reserve is publishing this proposed rule that would amend Regulation Z to implement certain amendments made by the Dodd-Frank Act. Regulation Z currently requires creditors to establish escrow accounts for higher-priced mortgage loans secured by a first lien on a dwelling. The proposal would implement statutory changes made by the Dodd-Frank Act that lengthen the time for which a mandatory escrow account established for a higher-priced mortgage loan must be maintained. The proposed amendments also would implement the Dodd-Frank Act's disclosure requirements regarding escrow accounts. Furthermore, the proposed rule would exempt certain loans from the Regulation Z escrow requirements. The exemption would apply to mortgage loans extended by creditors that operate predominantly in rural or underserved areas, originate a limited number of mortgage loans, and do not maintain escrow accounts for any mortgage loans they originate or service.

Summary of Comments

Below is a summary of ICBA's comments detailed in this letter:

- The Federal Reserve should consider the business and resources of community banks when crafting additional regulatory requirements, so that the costs and burdens of further regulation will not drive community banks out of the mortgage market.

- The Federal Reserve's proposed escrow disclosures should be integrated with the combined TILA and Real Estate Settlement Procedures Act (RESPA) disclosure that is currently being created by the Consumer Financial Protection Bureau (CFPB).

[2] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

- The Federal Reserve should not implement the transaction coverage rate at this time, and should instead allow the CFPB to examine this issue as they complete the review of the Regulation Z closed-end loan provisions and coordinate the TILA and RESPA disclosures.

- The Federal Reserve should allow consumers to waive the three-day waiting period in the instance of a bona fide personal financial emergency, and whether the consumer's emergency is a bona-fide personal financial emergency should be determined at the discretion of the financial institution.

- The Federal Reserve should exempt portfolio loans from the escrow requirements for higher-priced mortgage loans, because it is a more practical solution and is consistent with the intent of Congress.

- The exemption requirement that creditors must have made, during the preceding calendar year, more than 50 percent of their total first lien, higher-priced mortgage loans in counties designated by the Federal Reserve as "rural" or "underserved" is unworkable, and should not be criteria for determining whether a creditor is exempt from the Regulation Z escrow requirements.

- If the Federal Reserve sets a loan threshold for an exemption from the escrow requirements for higher-priced mortgage loans, it should be that a creditor cannot have originated and retained the servicing rights to more than 500 loans secured by a first lien on real property or a dwelling. A threshold of 100 or fewer loans is too low of a threshold for an exemption.

- The exemption requirement that creditors not service escrow accounts should be eliminated. This provision unfairly punishes the community banks that implemented escrow accounts based on the Federal Reserve's Regulation Z requirements that became effective on April 1, 2010.

The Business of Community Banks

ICBA understands the purpose in revising Regulation Z to regulate escrow accounts for closed-end mortgage loans, and appreciates the Federal Reserve's efforts in incorporating consumer testing in producing model forms that can be used. ICBA also understands the Federal Reserve's motivation in bolstering many Regulation Z provisions to address issues presented in the recent mortgage crisis, and its eagerness to further regulate financial institutions that

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engaged in irresponsible lending practices that led to our current economic state. Nevertheless, when drafting final amendments to Regulation Z, ICBA urges the Federal Reserve to consider the fact that community banks have always engaged in responsible mortgage lending practices due to their vested interest in their communities and the consumers they serve.

Furthermore, many community bank mortgage loans are held in portfolio and are not sold on the secondary market; therefore the underwriting for these loans has historically been more conservative since the banks have a vested interest in how the loans perform. Community banks also take great time to educate and inform their customers about the consequences of their borrowing decisions because of the banks' vested interest in the performance of these loans and the more familiar relationship community bankers have with their customers.

In addition, for many community banks, mortgage loan transactions are often not the cookie-cutter loan transactions found in the suburban and urban markets where there are rows and rows of similar houses. Many times, community bank mortgage loans are to consumers who have a unique situation, because of the various sizes of acreages, potential for a manufactured home deal, or the atypical location of the home. These situations do not fit the typical 30-year mortgage loan model because of the atypical nature of the property and the consumer's financial situation. Community banks are especially adaptable at making such loans because the bankers know their customers and community members, and have extensive knowledge of the home properties. Nevertheless, because these are atypical properties, they are frequently loans that would be considered "higher-priced" under the Regulation Z definition, thereby triggering the additional requirements.

ICBA strongly urges the Federal Reserve to consider the differences between community banks and large national financial institutions when crafting final rules. The Federal Reserve should not punish community banks with harsh regulatory changes that will restrict their ability to lend to the consumers in their communities thereby making these consumers more dependent on the larger financial institutions that care more about profits than the financial health of the communities they serve. The reality is, the more regulatory changes that are forced onto community banks, the harder it will be for these banks to compete and offer loan products. Many community banks are currently understaffed and overworked, and their compliance resources must be considered when crafting additional regulatory requirements.

The Federal Reserve's Proposed Escrow Disclosures Should Be Integrated in the TILA/RESPA Disclosures

The Federal Reserve is proposing new disclosures regarding escrow requirements for consumers. However, this proposed rule is not accompanied by a Department of Housing and Urban Development (HUD) proposal to eliminate the RESPA disclosures on escrow accounts once the Federal Reserve's proposed rule becomes final, which means the RESPA disclosures would continue to be required and the Federal Reserve's proposed TILA disclosures explaining escrow accounts would be duplicative. This disclosure scheme is not practical considering consumers are already overwhelmed with mortgage disclosures and are therefore not paying attention to the disclosures that are important and need their consideration.

Furthermore, the CFPB is in the process of integrating both the TILA and RESPA disclosures into one disclosure document, as mandated by Congress in the Dodd-Frank Act. Elizabeth Warren, Assistant to the President and Special Advisor to the Secretary of the Treasury on the CFPB, has stated publicly that the CFPB's TILA/RESPA integration project is among its top priorities, and the CFPB has already begun the project even though they have not yet assumed rule writing authority over TILA and RESPA.

Based on the circumstances, ICBA strongly urges the Federal Reserve not to require additional escrow disclosures at this time, and instead to allow the CFPB to review and write rules to coordinate all mortgage disclosures as it pursues the integration of the disclosures required by TILA and RESPA. This rulemaking strategy is consistent with the Federal Reserve's own press release announcement made on February 1, 2011:

> [The Federal Reserve Board] has carefully evaluated whether there would be public benefit in proceeding with the rulemakings initiated with the Board's August 2009 and September 2010 proposals at this time. Because the Board's 2009 and 2010 TILA proposals would substantially revise the disclosures for mortgage transactions, any new disclosures adopted by the Board would be subject to the CFPB's further revision in carrying out its mandate to combine the TILA and RESPA disclosures. In addition, a combined TILA-RESPA disclosure rule could well be proposed by the CFPB before any new disclosure requirements issued by the Board could be fully implemented. For these reasons, the Board has determined that proceeding with the 2009 and 2010 proposals would not be in the public interest. Although there are specific provisions of this Board proposal that would not be affected by the CFPB's development of joint TILA-RESPA disclosures, adopting those portions of the Board's proposal in a

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piecemeal fashion would be of limited benefit, and the issuance of multiple rules with different implementation periods would create compliance difficulties.

Requiring community banks to provide duplicative disclosures that may soon be made obsolete by future CFPB regulatory requirements is extremely burdensome and confusing. A far more productive approach would be to allow all of the mortgage disclosures to be coordinated and regulated by the CFPB, which has already started the TILA/RESPA integration project. If regulatory requirements on all the mortgage disclosures are promulgated at one time instead of in a piecemeal fashion, compliance will be easier for community banks and disclosures will be more streamlined for consumers.

The Federal Reserve Should Not Implement the Transaction Coverage Rate at this Time

The Federal Reserve is also proposing in this rulemaking to use a transaction coverage rate in a comparison to the average prime offer rate (APOR) for purposes of defining which loans would be considered "higher-priced mortgage loans" which would require escrow accounts. Under the current Regulation Z, a higher-priced mortgage loan is defined by comparing the loan's annual percentage rate (APR) to the current APOR. Under the Dodd-Frank Act requirements, this measurement is also used for defining which loans would require escrow accounts.

The Federal Reserve is proposing to use a loan pricing benchmark that would be the transaction coverage rate rather than the APR. The Federal Reserve previously proposed this comparison in its 2010 Regulation Z proposed rule, which it later stated on February 1, 2011, it would not finalize and would instead allow the CFPB to finish. In this current Federal Reserve proposed rule, the agency is again proposing to use the transaction coverage rate as the comparison to the APOR. The transaction coverage rate would be the APR calculated without prepaid finance charges unless the creditor, mortgage broker, or an affiliate of either retains the charges.

ICBA strongly urges the Federal Reserve not to alter the provisions for determining higher-priced mortgage loans and to allow the CFPB to revisit this issue as they finish the Regulation Z mortgage rulemaking and TILA/RESPA integration project. Providing such massive changes to these rate calculation rules in a piecemeal fashion is incredibly confusing and burdensome to community banks, and is a project that should be conducted simultaneously with the other regulatory changes being pursued by the CFPB.

Consumer's Waiver of Waiting Period Before Consummation

The Dodd-Frank Act requires disclosures and a three day waiting period before consummation of a loan if an escrow account is required for the mortgage loan.[3] Proposed § 226.19(f)(6) would permit consumers to modify or waive the three business day waiting period following receipt of the escrow account disclosures required, for bona fide personal financial emergencies. The proposed provisions would require the consumer waiving the waiting period to give the creditor a dated, written statement that describes the emergency, specifically modifies or waives the waiting period, and bears the signature of all consumers primarily liable on the legal obligation. Printed waiver forms could not be used.

To qualify as a bona fide personal financial emergency, the proposed requirements state the situation must require disbursement of loan proceeds before the end of the waiting period. The proposed provision further clarifies that a bona fide personal financial emergency typically will involve imminent loss of or harm to a dwelling or harm to the health and safely of a natural person.

ICBA believes that some consumers may be harmed by waiting three business days after receiving their escrow disclosure before proceeding with their mortgage loan transaction. While the bona fide exemption is intended to provide some relief, the standard is so difficult to satisfy, that no community banks would be comfortable relying on their interpretation of the exclusion, and would instead have a hard policy that requires the three day waiting period in all instances. As the proposed rule currently reads:

> Whether there is a bona fide personal financial emergency is determined by the facts surrounding the individual circumstances. A bona fide personal financial emergency typically, but not always, will involve imminent loss of or harm to a dwelling or harm to the health or safety of a natural person. A waiver is not effective if the consumer's statement is inconsistent with facts known to the creditor.[4]

Based on this language, the creditor would have to investigate whether the facts at the time are consistent with the statements provided by the consumer. Community banks would take time and effort to insure regulatory compliance with this waiver requirement, in which case the time taken would likely exceed the three day waiting period, rendering this bona fide personal financial emergency exception meaningless.

[3] Dodd-Frank Act § 1461(a), TILA § 129D(h).
[4] Proposed 12 CFR 226.19(f)(6)-2.

Therefore, ICBA urges the Federal Reserve to allow consumers to waive the three day waiting period in the instance of a bona fide personal financial emergency, and whether their emergency should be considered a bona fide personal financial emergency should be determined at the discretion of the financial institution. The detailed standard, as outlined by the Federal Reserve, should be changed to allow financial institutions the discretion of allowing this waiver in emergency circumstances, without having the burden of verifying all the facts of the consumer's particular emergency, which would take at least three business days to determine.

For refinancings, ICBA urges the Federal Reserve not to require any additional waiting period for escrow accounts, but to allow the waiting period to run concurrently with the rescission waiting period.

Exemption from Escrow Account for Higher-Priced Mortgage Loans

Under the current Regulation Z, a creditor may not extend a higher-priced mortgage loan secured by a first lien on a consumer's principal dwelling unless an escrow account is established before consummation for payment or property taxes and insurance. Under TILA § 129D(c), which was added by Congress in the Dodd-Frank Act, § 1461, the Federal Reserve is authorized to exempt from the escrow requirement a creditor that (1) operates predominantly in rural or underserved areas; (2) together with all affiliates has total annual mortgage loan originations that do not exceed a limit set by the Federal Reserve; (3) retains its mortgage loan originations in portfolio; and meets any asset-size threshold and any other criteria the Federal Reserve may establish.

In this proposed rule, the Federal Reserve is proposing to exempt any creditor from the escrow requirements for higher-priced mortgage loans if the creditor satisfies the following criteria: (1) the creditor makes most of its first-lien higher-priced mortgage loans in counties designated by the Federal Reserve as "rural or underserved,"; (2) together with its affiliates originates and services 100 or fewer first-lien mortgage loans; and (3) together with its affiliates does not escrow for any mortgage loan it services.

While ICBA is pleased that the Federal Reserve is, consistent with the mandate of the Dodd-Frank Act, providing an exemption for banks from the escrow requirements for higher-priced mortgage loans, we strongly believe that the exemption should be more inclusive and should include all financial institutions that hold their mortgage loans in portfolio until the loan matures or is sold or refinanced. ICBA urges the Federal Reserve to provide this more inclusive exemption for financial institutions as soon as possible. This provision, unlike the disclosure requirements for escrow accounts, need not wait until the CFPB

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reviews the Regulation Z mortgage provisions and TILA and RESPA disclosures.

The Current Regulation Z Escrow Requirements Have Been Damaging for Community Banks and their Customers

Before the Federal Reserve's escrow requirements for higher-priced mortgage loans became effective in April 2010, many community banks did not provide escrow accounts for residential mortgage loans. Because many community banks did not have the resources to escrow for mortgage loans in house or the loan volume to outsource this servicing, the new amendments have required many community banks to dramatically change their mortgage business, which has greatly affected their customers.

The Federal Reserve's new escrow requirements have been particularly daunting, given the current interest rate environment where a higher-priced mortgage loan under the Federal Reserve's established threshold would have an annual percentage rate of less than 6.5 percent for a first lien mortgage. As a result of the current escrow requirements under Regulation Z, many community banks have had to severely limit or eliminate their consumer mortgage business.

The Federal Reserve's escrow requirements for higher-priced mortgage loans have particularly disabled community banks that offer atypical loans or loans with small principal amounts, which has meant fewer or limited opportunities for customers who would normally qualify for a loan to be able to purchase a home. Furthermore, many larger lenders are unwilling to make these types of loans, so the access to credit has completely dried up for a segment of the consumer population.

The extensive regulatory requirements of not only Regulation Z, but the Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act) and RESPA, have prevented even some community banks from offering mortgage loans with lower principal loan amounts. For example, one community banker told ICBA that most of their residential real estate loans are less than $25,000. Due to the smaller loan amounts and the amount of extensive regulatory requirements they have been faced with, the smaller dollar loans are no longer profitable for them to provide. This has greatly limited the access to credit for the consumers in their community, a result that ICBA does not believe was intended by the regulators.

Based on an ICBA Survey of approximately 677 community banks, recently conducted in April 2011, only 16 percent of community bank respondents stated that the Federal Reserve's escrow requirements had no negative impact on their bank's residential mortgage lending. Thirty-one percent of community bank respondents stated they implemented the escrow system but either passed the increased costs on to consumers, reduced their loan volume, or both. An additional 37 percent of community bank respondents completely stopped making the types of mortgages that would trigger the Regulation Z escrow requirements.

For community banks that have decreased the amount of higher-priced mortgage loans they provide or eliminated making these loans altogether, 51 percent stated that borrowers in rural areas have been affected by this business change; whereas 38 percent replied that non-conforming borrowers were affected, and 32 percent responded that first-time home buyers were affected.[5]

Community Bank Portfolio Loans Should be Exempt from the Escrow Requirements for Higher-Priced Mortgage Loans

The Federal Reserve's proposed exemption to these escrow requirements will provide very little relief to community banks and their customers. While, ICBA appreciates the efforts of the Federal Reserve staff in exempting certain financial institutions from the escrow requirements for higher-priced mortgage loans, we strongly urge the Federal Reserve to adopt an exemption to the escrow requirements for financial institutions that hold their mortgage loans in portfolio.

Since many community banks hold their mortgage loans in portfolio for the life of the loan, they have a vested interest in how the mortgage loan performs and the consumer's ability to repay, not only their loan amount, but the property taxes and insurance. Based on ICBA's recent survey, 51 percent of the community bank respondents stated that 100 percent of the residential mortgage loans they originate are retained in portfolio and serviced until the loan matures or is repaid. An additional 17 percent of community banks replied that over 75 percent of the mortgage loans they originate are held in portfolio by the bank.[6]

Moreover, Congress has requested the Federal Reserve to allow an exemption from the Regulation Z escrow requirements for portfolio loans. The exemption was expressly provided for under TILA § 129D(c), which was added by Congress in the Dodd-Frank Act, § 1461. Members of Congress also expressed this sentiment to the Federal Reserve in a letter sent to Governor Elizabeth Duke on March 18, 2010, in which 31 members of Congress urged the Federal Reserve to exempt mortgage loans originated and held by depository institutions in portfolio from the Regulation Z escrow requirement for higher-priced mortgage loans.

[5] *See* Appendix A.
[6] *Id.*

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ICBA is concerned that the Federal Reserve is not considering the wishes of Congress in providing this exemption for mortgage loans that are held in portfolio by financial institutions, and strongly urges this exemption be provided consistent with the request from Congress. While the Federal Reserve's current proposed exemption provisions may provide a small amount of relief to community banks, as explained more fully below, it is not an effective solution. An exemption for portfolio loans would be an effective solution.

Community Bank Customers Do Not Favor Escrow Accounts

ICBA supports an exemption from the escrow requirements for community bank portfolio loans because of the resources entailed in setting up escrow accounts, and particularly, because mandatory escrow accounts have been found to be unnecessary for purposes of protecting community bank customers. As stated previously in this letter, community banks operate a different business model than larger financial institutions. Community banks have close relationships and active communication with their customers. Community bankers know their customers personally, interact with them in the community, and therefore have a vested interest in their financial situation and loan status. Because community banks often retain mortgage loans in portfolio, they make every effort to insure that customers are able to pay their mortgage loans, taxes, and insurance, and the loans are therefore more solidly underwritten.

Aside from being an unnecessary consumer protection, many community bankers have told us that their customers do not prefer having escrow accounts for their first lien mortgage loans. Based on ICBA's recent survey regarding escrow accounts, only 4 percent of the community bankers said that their customers are generally in favor of having escrow accounts on their loans. Almost 40 percent of the community bankers said that their customers do not prefer having an escrow account and would rather pay their taxes and insurance directly. An additional 37 percent of bankers responded that the feeling regarding escrow accounts varied among the customers.[7]

Some community bankers have commented that because their customers are not accustomed to escrow accounts, they feel apprehensive about setting up the accounts, and feel as though the bank is "making" them do something that is not in their best interest. Also, many loans in rural areas have small principal balances, and some community bankers have expressed that their customers are not happy with having an escrow account for a low loan amount. One example provided to ICBA was a mortgage loan where the loan principal amount was $15,000, which is less than many automobile loans. Because the rural area

[7] *See* Appendix A.

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also had a low tax, the amount of money the customer was required to escrow was $250. A federal requirement to escrow for this amount seems ridiculous, and has perplexed many community bankers and their customers.

The Proposed Escrow Exemption for Higher-Priced Mortgage Loans is not Effective

There are problems with the Federal Reserve's proposed escrow exemption that render it completely ineffective. ICBA's comments on the specific exemption provisions are as follows:

Definitions of "rural" and "underserved" are not workable.

Under the Federal Reserve's proposed exemption provisions, a creditor must have made, during the preceding calendar year, more than 50 percent of its total first lien, higher-priced mortgage loans in counties designated by the Federal Reserve as "rural" or "underserved." The Federal Reserve proposes extensive criteria for what would be considered "rural" or underserved."

ICBA opposes this specific requirement for several reasons. First, the measurement for determining what is considered a "rural" or "underserved" area is extensive and confusing, which could have the effect of community banks making the assumption that they may not satisfy this definition even if they do. In today's environment of rigorous bank examinations, community banks have taken a conservative approach to regulatory compliance, for fear that a minor or technical error could lead to a violation. This is especially the reality in today's confusing environment of frequent and piecemeal regulatory changes on mortgage lending.

Notwithstanding these proposed regulatory requirements, ICBA is hearing from some bankers that the current mortgage rules are so extensive and difficult to comply with, that they consider providing mortgage loans to be a compliance liability. ICBA has heard from community bankers that even bank internal auditors are unsure of how to properly comply with many of the new Regulation Z mortgage provisions. These are companies where regulatory compliance is their primary business. While the Federal Reserve's exemption attempts to make business easier for community banks by providing relief from the escrow requirements, we doubt that many community banks will utilize the exemption for fear they may not satisfy the detailed requirements.

Second, ICBA believes it is bad public policy to put financial institutions in the position of monitoring where exactly they are providing most of their mortgage loans so they can insure they qualify for an exemption from further regulatory requirements. They should not have to incur one burden to avoid another. Community banks, by nature, operate in smaller and often rural communities, and provide a service their customers may not be able to obtain elsewhere. Community banks should not be inhibited from providing mortgage products to customers in certain areas, out of concern that they may not satisfy a regulatory exemption.

Furthermore, the proposed definitions of "rural" and "underserved" are too restrictive. The Federal Reserve defines "rural" as "not in a metropolitan statistical area or micropolitan statistical area, as those terms are defined by the U.S. Office of Management and Budget, and ... not adjacent to any metropolitan area or micropolitan area; or it is adjacent to a metropolitan area with fewer than one million residents or adjacent to a micropolitan area, and it contains no town with 2500 or more residents." This definition does not reflect the reality of many areas that would be considered rural. Micropolitan areas are not populous areas and these areas should be eligible for the escrow exemption. The rural definition is also very narrow because many low population areas would not be considered rural if they happen to be near a larger metropolitan area.

For example, ICBA has heard from member banks that there are few banks in Texas that would actually qualify for the rural designation, even though they are very much rural community banks. The reality is there are not very many counties in the United States that are not adjacent to metropolitan or micropolitan areas.

This proposed provision also ignores the fact that many rural areas with lower property values are located within a close vicinity to a metropolitan area. For example, ICBA has heard from community bankers in rural areas that are close to larger cities that the financial institutions in those larger cities do not want to make the smaller loans to the customers in their community because the smaller principal loans are not as profitable. We have found that community banks are frequently the go-to bank for mortgage loans that are small, such as under $50,000 principal amount, but these loans would not be exempt from the escrow requirements if the bank does not satisfy the location provision.

The proposed rule also provides an exemption for some mortgage loans provided in "underserved" counties, but defines a county as "underserved" if, during a calendar year, no more than two creditors extend consumer credit five or more times secured by a first lien on real property or a dwelling. This criterion puts community banks in the position of having to monitor not only their own loan volume, but the loan volume of other creditors within their vicinity. This is a very difficult standard to satisfy for a community bank, which will more likely stop providing higher-priced mortgage loans than take the risk that they are improperly satisfying the exemption requirements. Neither the "rural" nor the "underserved" definitions are workable or nearly as straight-forward to apply as an exemption for portfolio loans would be.

Threshold of 100 or fewer loans should be increased to 500 or fewer loans.

To obtain an exemption from the escrow requirements, a financial institution cannot have originated and retained the servicing rights to more than 100 loans secured by a first lien on real property or a dwelling during either of the preceding two calendar years. ICBA believes this threshold is much too low. If loan volume is used as criteria for an exemption from the escrow requirements, the Federal Reserve should increase the threshold to 500 loans secured by a first lien on real property or a dwelling.

The Federal Reserve staff has stated in discussions with ICBA staff that, in researching the outsourcing of escrow accounts, they were unable to find an outside servicer that would service escrow accounts for smaller community banks unless their loan volume was in the hundreds, far greater than 100 first lien mortgage loans. Therefore, the threshold set by the Federal Reserve should not be any lower than the volume of loans required for a smaller financial institution to cost effectively outsource this servicing.

Furthermore, this exemption requirement would not cover many community banks because of the low threshold amount. In ICBA's recent survey conducted of community banks, almost 40 percent of the bank respondents provide 100 or more first liens secured by property or a dwelling. That means that almost 40 percent of these community banks would not qualify for the exemption based on this criterion alone, without even considering whether they would qualify for the remaining exemption criteria.[8]

Also, if the de minimis loan volume is set too low, it puts community banks in the position of completely altering their business and the customers they serve in order to meet the exemption requirement. Setting the de minimis amount to 500 loans would capture the community banks that should be captured with this exemption.

Requirement of no previous escrow accounts should be eliminated.

ICBA is strongly opposed to the requirement that community banks must not service escrow accounts in order to qualify for the escrow exemption for higher-

[8] *See* Appendix A.

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priced mortgage loans. This exemption requirement is unfair to the community banks that have implemented escrow accounts, most on a limited basis. As the Federal Reserve is aware, community banks were required to implement escrow accounts for higher-priced mortgage loans, effective April 1, 2010. Many community banks that did not previously employ mortgage loan escrows under any circumstances were forced to either: a) implement escrows, or b) no longer provide higher-priced mortgage loans.

Rather than deny mortgage credit availability to their communities, many community banks chose to implement mortgage loan escrows, despite the cost and burden. Some of these community banks provided escrow accounts to a small and manageable number of consumers, but could not provide escrows to a broader number on a cost efficient basis. The proposed rule for the exemption, that "the creditor...must not maintain an escrow account for any mortgage loan they currently service," is thus inherently unfair to banks that chose to continue to service their communities and implement escrow accounts, despite the burden and cost. In fact, a financial institution that did not comply with the Federal Reserve's escrow requirements would actually benefit from their non-compliance based on this proposed exemption requirement. If the Federal Reserve intended to require this criterion for an exemption from the escrow requirements, it should have done so well before the April 1, 2010 effective date for setting up escrow accounts, so that community banks could have utilized the exemption instead of attempting to comply with the requirements.

As it is now, many community banks have tried to comply with the escrow requirements by absorbing the costs or limiting their loan volume. Based on ICBA's recent survey conducted of community banks, only 39 percent of the bankers responded that they do not have any escrow accounts for any of the residential mortgage loans they originate and service.[9] That means over 60 percent of the community banks would automatically not satisfy the Federal Reserve's escrow exemption. Of the 39 percent of banks that do not have escrow accounts, they would still have to satisfy the other exemption requirements, which are also difficult to satisfy, in order to obtain an exemption. This leads us to ponder how many community banks would actually qualify for this exemption as it is currently written, and whether the proposed exemption is even meaningful.

Based on the reasons expressed in this letter, ICBA strongly urges the Federal Reserve to revisit the escrow exemption for financial institutions and provide an exemption for higher-priced mortgage loans that are held in portfolio. This

[9] *See* Appendix A.

escrow requirement has and will continue to add tremendous operating costs for community banks, which will continue to negatively impact their customers.

ICBA thanks you for the opportunity to comment on this proposed rule. As you are aware, community banks are common-sense lenders that offer mortgage products on fair terms as a means of providing valuable services to their customers. In drafting any final amendments, please keep in mind that community banks care about customer service above all else, and have not engaged in the misleading practices that have motivated Congress and the federal agencies to further regulate the mortgage business.

If you have any questions about this letter or the attached survey, or need additional information, please do not hesitate to contact me at 202-659-8111 or Elizabeth.Eurgubian@icba.org. In addition, ICBA would be happy to meet with Federal Reserve staff to discuss these comments in further detail and provide additional insight from the community banker perspective.

Sincerely,

/s/

Elizabeth A. Eurgubian
Vice President & Regulatory Counsel

ICBA
INDEPENDENT COMMUN
BANKERS of AMERICA

Appendix A

ICBA Survey

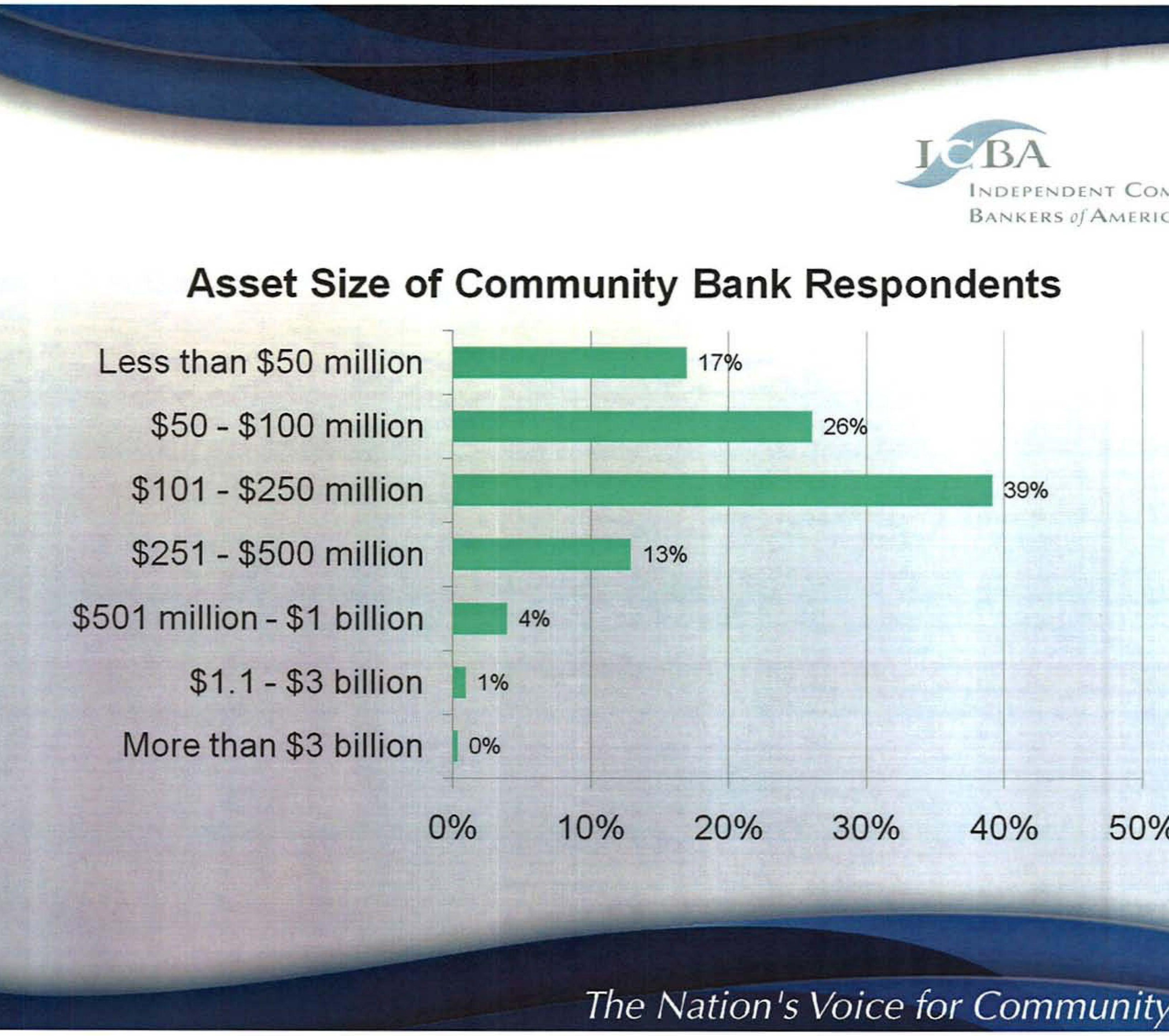
Escrow Requirements for Higher-Priced Mortgage Loans

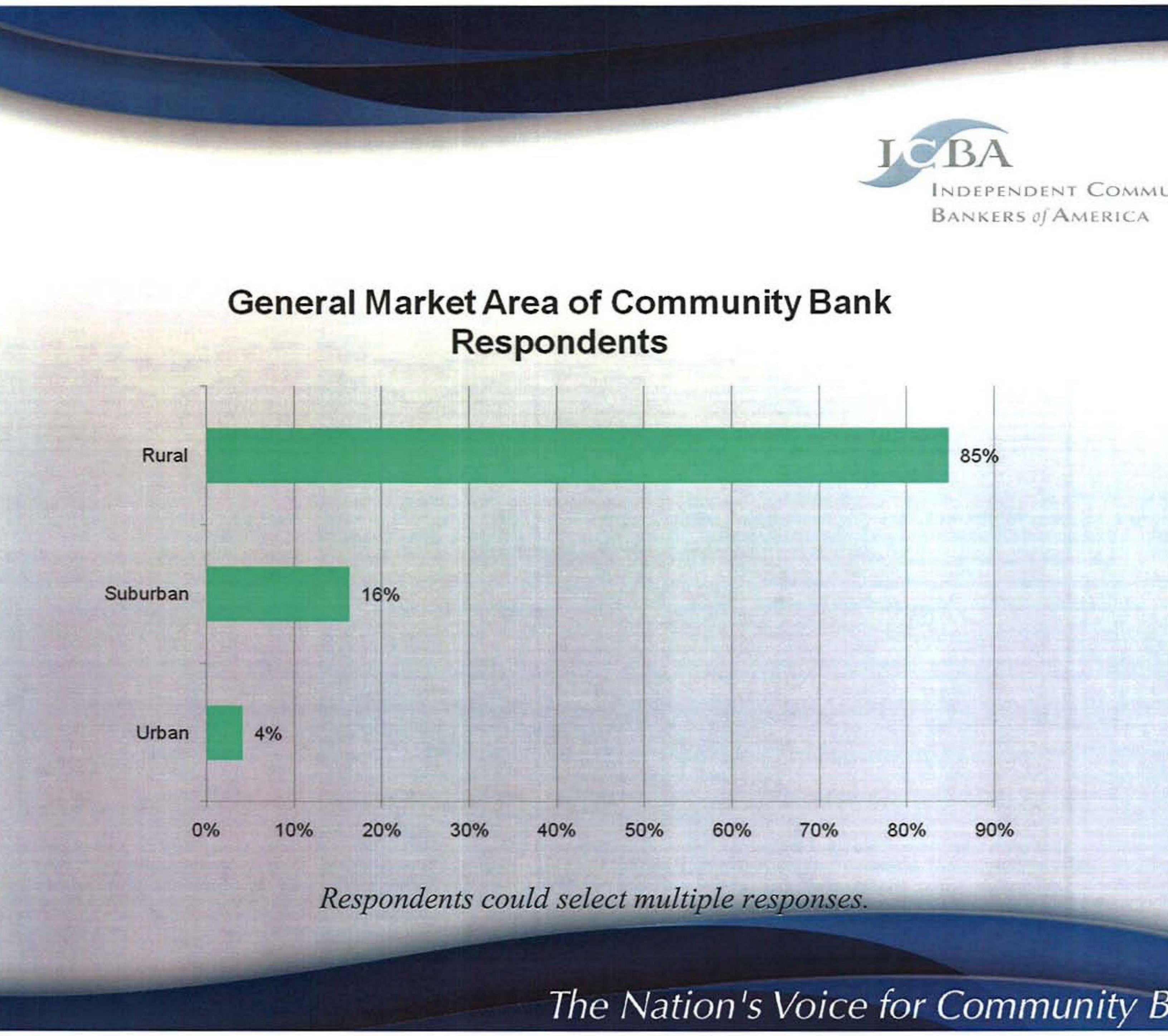
The Nation's Voice for Community Ba

Respondent Demographics

- 677 community bank respondents
- 85% of respondents operate in rural areas

Note: Percentages provided may not add exactly to 100% due to rounding.


ICBA
Independent Com
Bankers of Americ
Asset Size of Community Bank Respondents
Less than $50 million
$50 - $100 million
$101 - $250 million
$251 - $500 million
$501 million - $1 billion
$1.1 - $3 billion
More than $3 billion
17%
26%
39%
13%
4%
1%
0%
0%
10%
20%
30%
40%
50%
The Nation's Voice for Community


ICBA
INDEPENDENT COMMU
BANKERS of AMERICA
General Market Area of Community Bank Respondents
Rural
85%
Suburban
16%
Urban
4%
0%
10%
20%
30%
40%
50%
60%
70%
80%
90%
Respondents could select multiple responses.
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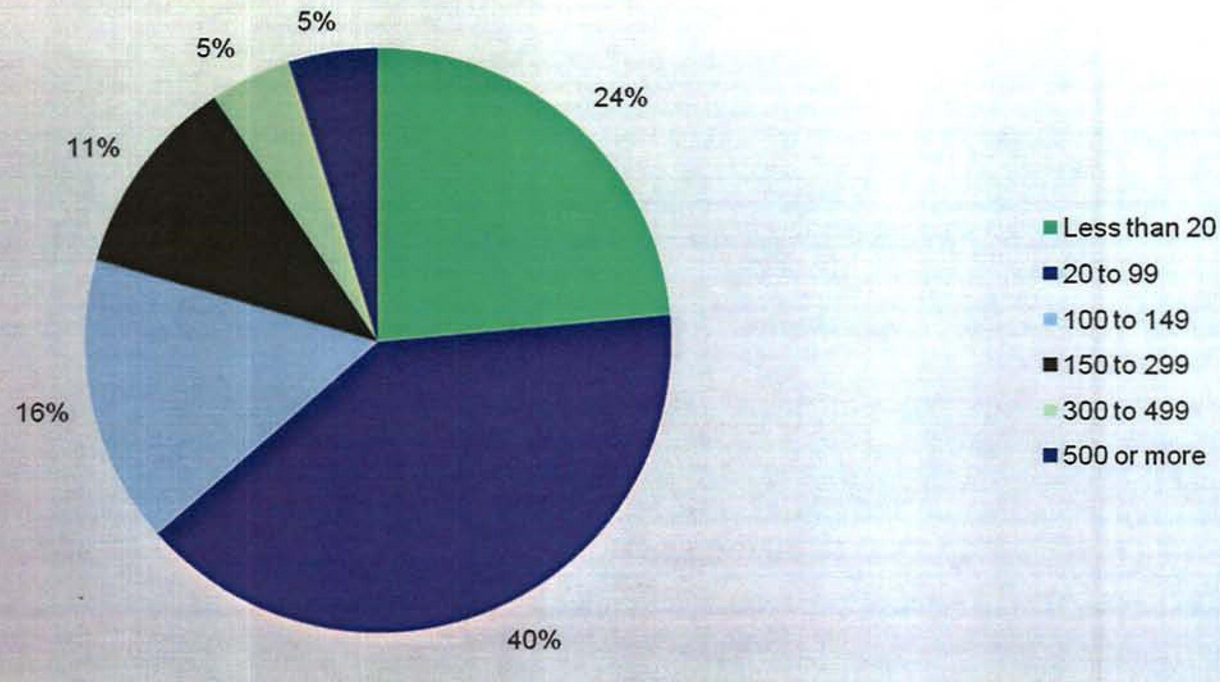
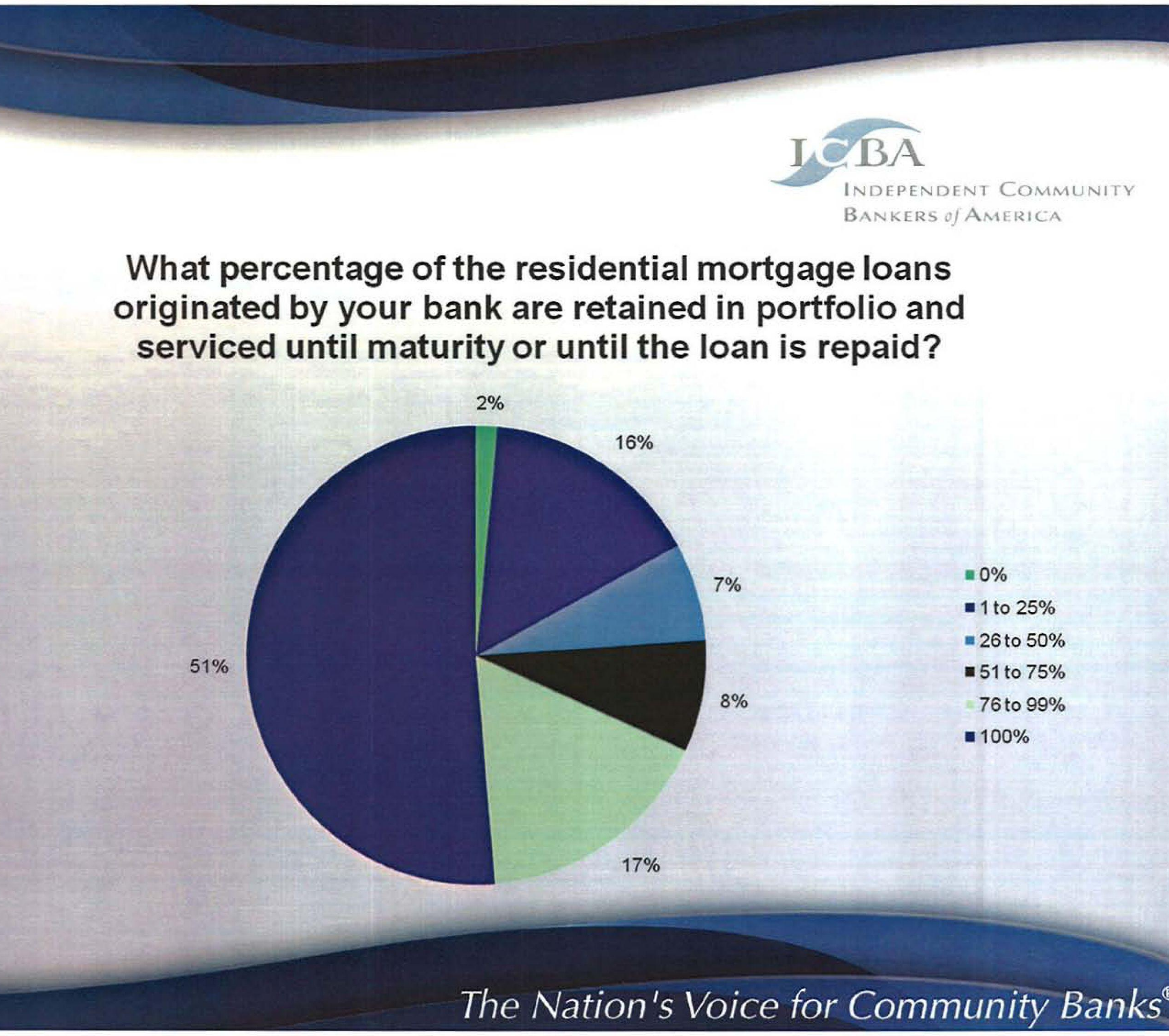
BANKERS of AMERICA

How many loans secured by a first lien on real property or a dwelling does your bank both originate and retain the servicing rights to annually?




ICBA
Independent Community Bankers of America
What percentage of the residential mortgage loans originated by your bank are retained in portfolio and serviced until maturity or until the loan is repaid?
2%
16%
7%
8%
17%
51%
0%
1 to 25%
26 to 50%
51 to 75%
76 to 99%
100%
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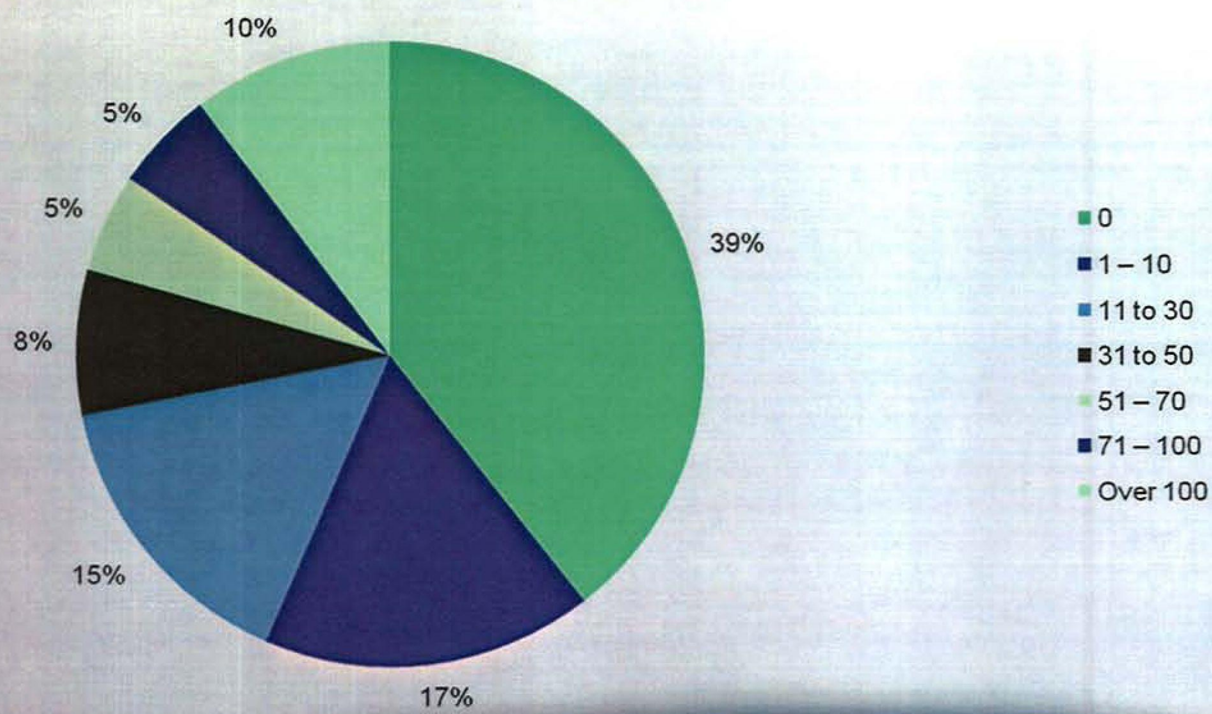
How many of the residential mortgage loans that your bank originates and services now have escrow accounts?



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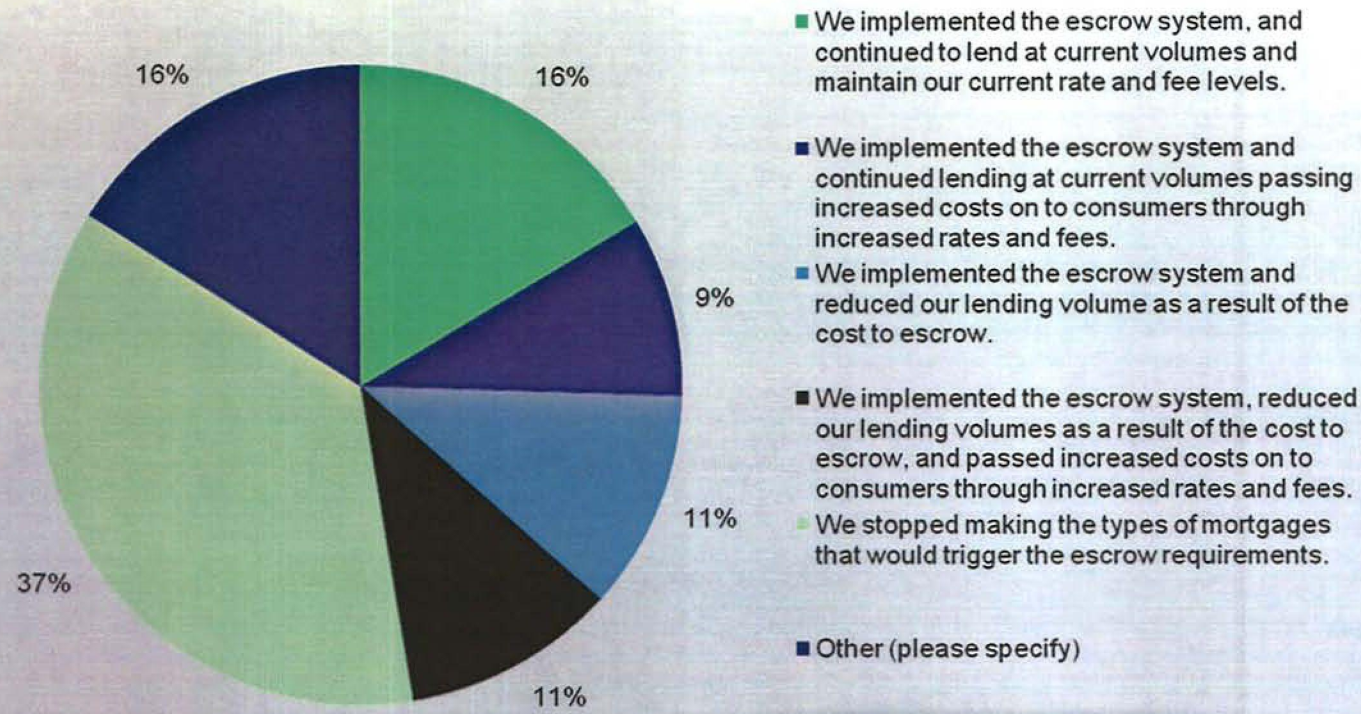
What effect has the Fed's escrow requirements for "higher-priced mortgage loans" had on your bank's residential mortgage lending?



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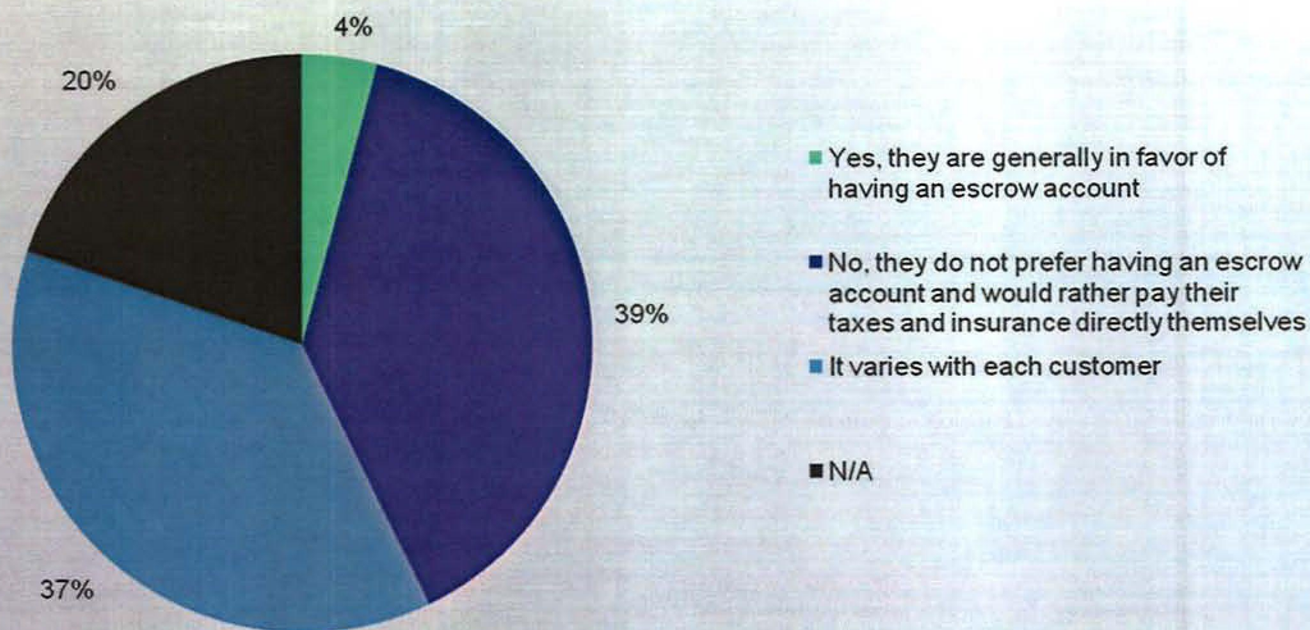
Based on any feedback received, do your customers who have "higher-priced mortgage loans" prefer the requirement that they escrow for taxes and insurance?



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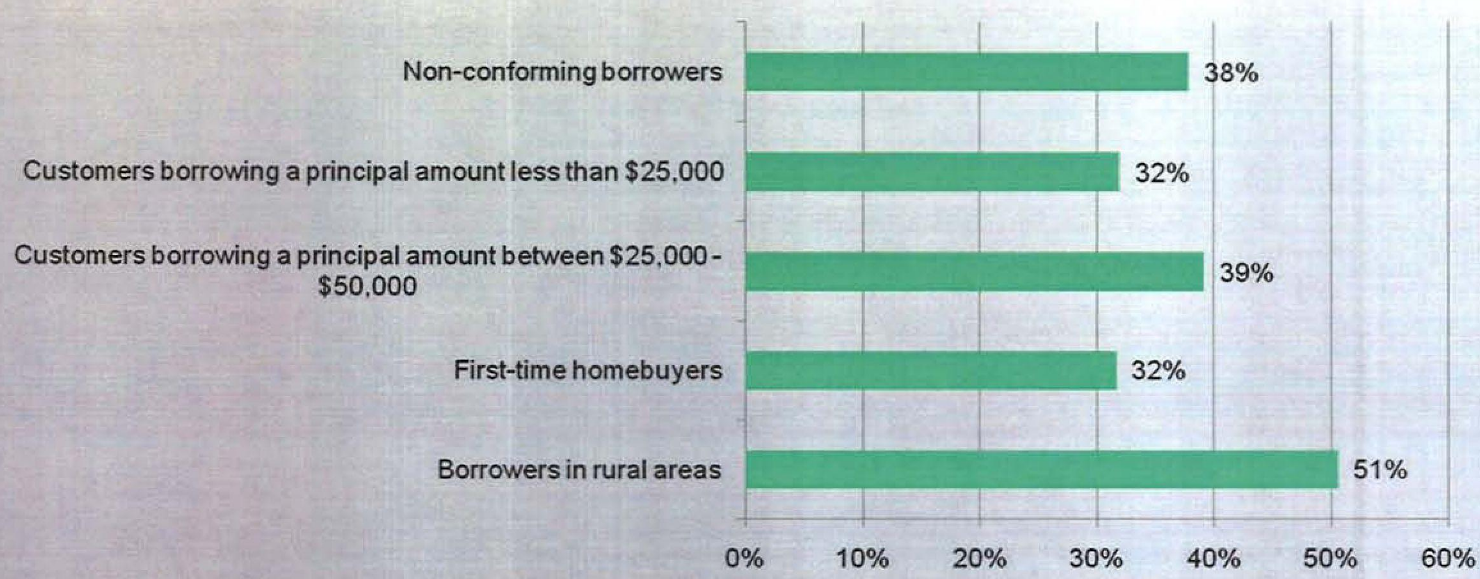
If your bank no longer makes mortgages that are "higher-priced mortgage loans" due to the Federal Reserve's new escrow requirements or has limited the amount of mortgages it provides, which customers have been impacted?



Respondents could select multiple responses.