NAVY FEDERAL Credit Union®

Office of the President

July 20, 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 Number OP-1288 Home Equity Lending Market

Dear Ms. Johnson:

Navy Federal Credit Union provides the following comments in connection with the public hearing held on June 14, 2007 by the Board of Governors of the Federal Reserve System (Board) to address the home equity lending market. Navy Federal is the nation's largest natural person credit union with $30 billion in assets and nearly 3 million members.

Generally, Navy Federal believes the financial services industry functions more effectively in a free market environment unencumbered with burdensome and costly regulatory constraints. Although certain rules may be necessary to adequately inform consumers and guard against abusive practices, a less regulated market encourages the development of a wider range of products and services to effectively and efficiently meet consumers' individual needs. Increased product offerings, however, may require greater sophistication to assure appropriate matching of offerings with consumers. Rather than promulgating rules that constrain marketplace offerings, we believe national policy should focus on improving the abilities of lenders, brokers, and consumers to match products with individual needs.

Recent guidance issued by the five primary federal regulators of financial institutions focuses on the characteristics and underwriting standards of certain mortgage products with a "one size fits all" approach. Such a standardized approach defeats the purpose of offering a broad array of mortgage products that could be tailored to each borrower's individual situation. The mortgage lending "guidance" of regulatory agencies will likely deny the benefits of home ownership to a significant number of consumers who seek and are in fact able to afford alternative mortgage products. Additionally, regulatory agencies' enforcement of the "guidance" as regulation exacerbates its negative impact on the mortgage market and consumer choices.

Although Navy Federal generally prefers less regulation, we believe the enforcement of "guidance" in the place of regulation creates compliance confusion, fosters misunderstandings of regulatory actions, and generally represents a disservice to the public. Further, the issuance of regulation as guidance is inconsistent with Executive Order 12866 and OMB's *Bulletin for*

PO Box 3000 Merrifield VA 22119-3000

Agency Good Guidance Practices (FR Vol. 72, p. 3432, January 25, 2007). We believe the recent "guidance" on mortgage lending rises to the level of regulation as defined in Executive Order 12866 and the *Bulletin for Agency Good Guidance Practices*. Our belief seems to be confirmed by the following comments by Ms. Julie Williams, First Senior Deputy Comptroller and Chief Counsel at the Office of the Comptroller of the Currency, in a July 11, 2007 speech before the New York Bankers Association; "[T]he guidance issued by the federal banking agencies extends only to the institutions that are supervised by federal regulators" and "[N]either type of guidance can be fully effective until it is adopted and actually applied by all states, not as a suggestion, but as *an expectation with consequences attached*" (emphasis added). Further, in its press release dated July 13, 2007, the Office of Federal Housing Enterprise Oversight stated, "OFHEO made this guidance applicable to Fannie Mae and Freddie Mac." OFHEO did not seek public comment before imposing rules on Fannie Mae and Freddie Mac that could affect thousands of consumers. If federal regulators generally expect regulated entities to abide by federal policy, the policy should be issued as regulation, not guidance, under established administrative procedures. Navy Federal urges all federal regulators to adhere to the Administrative Procedures Act and other formal directives when developing and implementing public policy involving providers and consumers of financial services.

The Board requested comments relating to several specific aspects of mortgage lending including prepayment penalties. We understand that unscrupulous lenders could entice borrowers with low teaser rates and entrap them in high cost loans with exorbitant prepayment penalties. Although Navy Federal does not advocate unnecessary regulation, we suggest that if the Board determines that prepayment penalties are abusive, it should follow the standard that Congress set for federal credit unions and prohibit the practice for all lenders. Section 107 of the Federal Credit Union Act stipulates that a borrower may repay his loan prior to maturity without penalty. We are not aware that the prohibition of prepayment penalties is a barrier to effective delivery of mortgage loans by federal credit unions.

Navy Federal believes the design of mortgage products and services as a matter of national policy will likely result in unintended or unforeseen problematic consequences. The decision to place taxes and insurance in escrow is best determined in the mortgage marketplace. Consumers and lenders should be free to determine whether escrow accounts meet their particular needs. Mandatory escrow accounts for certain mortgage products could create unnecessary burden and reduce payment options available to consumers. We strongly agree that consumers should not be misled about their responsibilities to pay taxes and insurance, whether as a portion of their mortgage payment or as a separate undertaking. Lenders should not be forced to become collection agents for taxing authorities and insurance companies.

Similarly, national policy should not specify the amount of documentation required for any particular mortgage loan. Appropriate "stated income" or "no doc" mortgage loans allow lenders to provide expeditious service to consumers who have mitigating factors, such as a combination of impeccable credit, low loan-to-value ratio, and other evidence of repayment ability. Lenders and borrowers agreeing to stated income and no doc loans share the responsibility of ensuring that the loan is appropriate for the particular situation.

We agree that lenders should have safe and sound underwriting policies to ensure that borrowers can afford a mortgage loan. However, the requirement to underwrite loans based on the fully indexed rate and the fully amortized payment amount will likely deny home ownership to some otherwise well-qualified borrowers. We believe there is a place in the market for nontraditional mortgage products, such as adjustable rate mortgages. For example, a military family who plans to stay in a home a short period of time may not need a fully indexed, fully amortizing mortgage. Also, individuals who expect increasing incomes, maturing investments, or any number of other repayment enhancing occurrences might very appropriately avail themselves to a nontraditional mortgage. We believe a national policy that requires all mortgages to be underwritten at fully indexed and fully amortized terms based on the applicant's current income is inappropriate and unnecessarily restrictive.

Increasing numbers of varied mortgage product offerings boost the need to assure that any particular loan is properly matched with the applicant. Both lenders and consumers share in this responsibility. Financial education improves consumer awareness of differing mortgage products and which products and services might be best for their personal financial needs. Public policy should support lenders and their efforts to improve the financial literacy of consumers by delivering, sponsoring, or otherwise supporting financial education efforts and programs.

Navy Federal appreciates the opportunity to comment on the adequacy of existing regulatory and legislative provisions on mortgage lending. If you have any questions with respect to our comments, please contact Shannon Tackett, Policy Analyst, at (703) 206-2577.

Sincerely,

John R. Peden
Acting President/CEO

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