CHASE

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August 15, 2007

Jennifer J. Johnson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Ave., NW
Washington, D.C. 20551
Attn: Docket No. OP-1288
Email:regs.comments@federalreserve.gov

Re: Federal Reserve System Docket No. OP-1288 - Notice of public hearing and request for comment.

JPMorgan Chase Bank, N.A. ("Chase") appreciates the opportunity to offer comment and to respond to the specific questions posed by the Board of Governors of the Federal Reserve System ("Board") at 75 Federal Register 30380 (May 31, 2007), with respect to the exercise of the Board's authority under the Truth in Lending Act ("TILA") to address certain lending practices. Chase strongly supports the Board's objective to address concerns regarding certain mortgage practices while preserving incentives for responsible lenders to provide mortgages to a wide array of borrowers.

This letter will: (i) set forth important considerations for the Board in the exercise of its authority under the TILA; (ii) comment on the Board's authority; (iii) offer recommendations; and (iv) respond to the specific questions asked by the Board.

At Chase, we are committed to helping our customers achieve and, more importantly, sustain home ownership. Key to our mission is properly evaluating our borrowers' ability and willingness to repay their mortgage with us. We have developed five fundamental principles to guide our business practices in home lending.

- We want our customers to be informed and able to make responsible choices based on their individual circumstances.
- We want to offer a broad array of mortgage products that address the financial needs and circumstances of our customers and provide good value at a competitive price.
- We want to be there if our customers suffer a life event and need our assistance to remain in their home.
- We want to provide support to strengthen and sustain the communities in which we live and work.
- Finally, we want to accomplish all of these things while providing a reasonable return to our investors on their commitment to this business.

Virtually everything we do is designed to support these guiding principles. We offer our comments with these principles in mind.

I. Important Considerations

Chase considers the following to be important considerations for the Board in contemplating the exercise of its authority under the TILA.

1. Reputable housing lenders strive to provide consumers with a broad range of mortgage products priced to reasonably reflect the risks associated with the borrower's credit profile, the loan collateral and the features of the mortgage product chosen. Lenders and investors have worked to balance risks and develop lending products and a secondary market that have greatly increased the availability of affordable credit to subprime borrowers who historically have had little to no credit availability and few, if any, product choices.

2. The availability of sophisticated credit scoring and historical credit information make for robust and highly predictive credit underwriting and have played a significant role in expanding the availability of credit to subprime borrowers. Risks, even layered risks, can be properly managed to enable lenders to serve the consumer need for subprime products without unduly restricting underwriting practices.

3. Lenders, secondary market investors and regulators have already taken action to address problems in the mortgage industry. The U.S. mortgage market has reacted quickly and credit has tightened significantly in America's mortgage market.

4. To minimize the negative impact on credit availability and product innovation, the Board should focus its actions only on the products and practices that create unreasonable risks. Safety and soundness and consumer protection concerns are considerably less significant in connection with mortgage products that do not result in significant payment shock shortly after origination.

5. Informed consumers who have undergone prudent underwriting reviews should not generally be denied access to the credit products that best serve their needs. Properly underwritten loan products that are adequately disclosed and well understood by borrowers are an acceptable credit risk. Requiring overly conservative underwriting standards that do not allow well informed borrowers to establish credit or grow into higher payments will eliminate the possibility of home ownership for many borrowers.

6. Payment increases have no negative impact when borrowers fully understand the terms of the loan products they acquire and are properly qualified with the ability to handle increased payments in the future. We urge the Regulators to recognize the benefits of reasonable payment caps and floors, prepayment fees and maturity dates, in creating affordable loan products for borrowers. Standard fixed rate products, even using extended maturity dates, do not offer borrowers sufficient product alternatives.

7. Regulatory actions that limit product choice or the availability of credit should be narrowly applied, recognizing that borrowers are best served by full disclosure of mortgage product features that allow for flexibility, choice and affordability.

8. Uniform, objective and clear regulatory standards promote both lender compliance and the efficient functioning of the secondary market.

9. To effectively address safety and soundness and consumer protection concerns, all mortgage lenders should be made subject to the same requirements, regardless of whether they are primarily regulated at the state or federal level. Limiting the scope of oversight to federally regulated lenders places them at a

competitive disadvantage, and does not entirely address concerns with respect to underwriting and disclosure practices in the mortgage market.

10. Adoption of the Nontraditional Mortgage Product Guidance and the Subprime Lending Statement by state agencies is not a solution to uniform application because state adoption does not ensure uniform interpretation and enforcement of the provisions. Uniform enforcement and implementation, which is essential to ensuring the competition required to provide the maximum benefit to consumers, can only be accomplished through federal regulation.

11. Since state regulated independent brokers are often the initial and predominant points of communication with borrowers, the ultimate lenders are unable to directly manage the brokers' marketing and application practices. Only uniform licensing, disclosure and training requirements can assure an adequate level of consumer protection.

12. Over 6 million borrowers, representing over $1.5 trillion in origination balances, will be experiencing loan resets in 2007 and beyond.[1] As a result, we anticipate that an unprecedented number of borrowers will be unable to qualify for loans underwritten in accordance with the terms of the Nontraditional Mortgage Product Guidance and the Subprime Lending Statement. This is exacerbated by the slow down in housing value appreciation. Therefore, lenders must be provided maximum flexibility to be able to effectively work with these borrowers to allow them to remain in their homes. These borrowers should not suffer the negative effects of a regulatory credit environment that did not exist when they obtained their loans.

II. AUTHORITY TO ACT

Pursuant to Section 105 and Section 129 of the TILA, the Board is authorized to address lending practices by all lenders in connection with residential mortgage loans.

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[1] First American CoreLogic, Inc., *Mortgage Payment Reset: The Issue and the Impact,* Christopher L. Cagan, Ph.D, (March 19, 2007), page 27.

Authority to promulgate disclosures: Any new disclosure requirements should be promulgated under Section 105(a) of the TILA. Section 129(l) of the TILA authorizes the Board to prohibit unfair or deceptive acts or practices, not to require new or additional disclosures. Only Section 105 expressly authorizes the Board to require new or different disclosures. The Board should clarify that any new disclosure requirements are promulgated pursuant to the Board's authority under Section 105 of the TILA.

Authority to prohibit unfair or deceptive acts or practices: Pursuant to Section 129(l)(2), the Board, by regulation or order, shall prohibit acts or practices in connection with (A) mortgage loans that the Board finds to be unfair, deceptive, or designed to evade the provisions of this section; and (B) refinancing of mortgage loans that the Board finds to be associated with abusive lending practices, or that are otherwise not in the interest of the borrower.[2] The authority of the Board is therefore limited to addressing lending practices that fall into these categories.

Previously, the Board has determined that an act or practice is unfair where it: (i) causes or is likely to cause substantial injury to consumers, (ii) cannot be reasonably avoided by consumers, and (iii) is not outweighed by countervailing benefits to consumers or to competition.[3] Public policy may also be considered in the analysis of whether a particular act or practice is unfair.[4] Finally, the Board has determined that an act or omission is deceptive if: (i) the act or omission misleads or is likely to mislead the consumer; (ii) the consumer's interpretation is reasonable under the circumstances, and (iii) the consumer's erroneous understanding is material.[5]

Given the authority and precedent set forth above, the Board's focus must be on preventing unfair and deceptive lending practices, rather than on prohibiting

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2 15 USC 1639, Section 129(l)(2).

3 Board of Governors of the Federal Reserve System & Federal Deposit Insurance Corporation, Unfair or Deceptive Acts or Practices by State-Chartered Banks (March 11, 2004); FTC Policy Statement on Unfairness (December 17, 1980), FTC Policy on Deception (October 14, 1983).

4 Id.

5 Id.

features that are not inherently unfair or deceptive. Clear, simple and effective disclosures go a long way towards allowing borrowers to make informed decisions, thereby allowing them to reasonably avoid features they do not desire, and thus, such features when properly disclosed should not be considered unfair or deceptive.

A violation of a requirement of Section 129 of the TILA may be subject to enhanced damages, including an extended right of rescission. Section 5 of the Federal Trade Commission Act, as well as state laws prohibiting unfair and deceptive acts and practices may also consider the failure to comply with a requirement of Section 129 as a violation subjecting lenders to substantial damages. The risks of such penalties and the potential for costly litigation, greatly reduce the availability and affordability of mortgage credit, as lenders decide that, because of these risks, particular products or features are not worth offering. Therefore, the Board's actions should be taken specifically and judiciously. The Board should clarify that any new or different disclosures are promulgated only under the authority of Section 105 of the TILA. In addition, any failure to comply should be determined to be "material" based only upon an individual evaluation of the facts and circumstances associated with a particular borrower.

III. RECOMMENDATIONS

To ensure uniform application and enforcement across all sectors of the mortgage industry, Chase supports the issuance of regulations calling for: (i) streamlined, clear and balanced disclosures at the shopping phase, three days after application and at closing, under the provisions of Section 105 of the TILA; and (ii) restrictions on certain underwriting practices with respect to particular classes of ARM loans that have significant potential for payment shock and on prepayment fees that extend beyond the initial reset period, under Section 129 of the TILA. Specifically:

Disclosure Requirements. Disclosure requirements should be streamlined, apply uniformly to all lenders and brokers, and be set forth in specific preemptive regulations, rather than in guidance, so as to ensure the consistency and quality of the disclosures. Chase recommends the following with respect to disclosures.

1. *Proper use of required disclosures must provide a safe harbor to lenders. Disclosures should be offered in general non-loan specific form at the*

shopping phase and in loan specific form shortly after application and at closing. Disclosures should address loan terms, payment shock, the potential for negative amortization, the terms of prepayment penalties, the costs of reduced documentation, the availability of escrow accounts, and the responsibility for payment of taxes and insurance.

2. *Chase suggests that required upfront shopping phase disclosures be provided as responses to a limited set of simple questions addressing key features of the loan products offered (e.g., Will my payment or interest rate increase throughout the term of my loan? Will my monthly payment cover only the interest accrued during the month at any time during the term of my loan? Can my loan balance go up, even if I make all required payments on time? Will my monthly payment include funds for taxes and insurance? If I choose to provide less documentation in the underwriting of my loan, will I pay additional costs? Will I pay an additional fee if the loan balance is paid off in whole or in part ahead of schedule?). This question and answer format would be much more helpful to a borrower than would be a comparison of worst case loan scenarios, none of which may be an accurate reflection of the borrowers own loan. Disclosure in a question and answer format, housed in a conspicuous box and offered in more than one language would operate as a simple and effective "nutrition label" for loan products.*

3. *Loan specific disclosures should be offered through revised initial and final TILA disclosure statements allowing for: (i) clarified disclosure of changes in monthly payments (such as bringing the initial monthly payment amount into the federal box with an express reference to the payment box for changes in future monthly payment amounts); (ii) clarification of whether or not the monthly payment amount includes an escrowed amount for payment of taxes and insurance when due; (iii) enhanced information with respect to the provisions for any prepayment fee; and, (iv) reference to the potential payment of additional fees at the time of any refinance. In addition, the Board should address the voluminous, duplicative and often confusing disclosures required under both the TILA and the Real Estate Settlement Procedures Act ("RESPA").*

Product Restrictions. Chase supports a prohibition on qualifying subprime borrowers based solely on aggressive short term teaser rates. However, initial market rates in effect for more than three years should not be characterized as "teaser rates," when coupled with reasonable periodic payment caps. To that end, Chase recommends the following limitations.

1. *Chase strongly recommends limiting application of a regulation requiring a determination of a borrower's ability to repay based upon a fully indexed rate and a fully amortizing payment to "Payment Shock Loans." Payment Shock Loans are closed-end ARMs in which during the initial 37 months of the term, either (i) any single scheduled payment amount is subject to an increase of more than thirty percent over the immediately preceding scheduled payment amount; or (ii) the cumulative increase in scheduled payment amounts is more than fifty percent over the initial scheduled payment amount. For purposes of this definition, scheduled payment amounts should not include amounts for taxes, insurance or other property assessments over which the lender has no control.*

2. *With respect to prepayment fees, Chase supports a restriction on substantial prepayment fees that extend beyond the initial interest rate adjustment period and a requirement that lenders provide a reasonable time (equal to sixty days prior to the initial payment reset date) to refinance without penalty.*

Given the two to four year average life of a subprime loan, many borrowers in adjustable rate products will never experience any form of payment shock. The relatively short average life of a mortgage loan minimizes the difference between adjustable rate mortgage loans and thirty year amortizing mortgage loans, as the principal reduction in the early years of a loan is quite small. *Should the Board promulgate any restrictions on ARM loans with initial payment reset periods in excess of 37 months, it should also clarify that in evaluating the unique aspects of a borrower's credit profile and overall financial characteristics, a creditor may give due consideration to the recognition of the potential for future gains in income and the effect of interest rate caps.*

We strongly recommend excluding mortgage loans above the agency conforming market thresholds ("Jumbo" mortgages), home equity loans, and home equity lines of credit. Jumbo borrowers are more sophisticated and better equipped to understand and effectively utilize mortgage products. Home equity loans and lines of credit have long been subject to existing guidance unique to the product. Home equity and Jumbo customers have long taken successful advantage of products offering cash flow management options as part of their overall financial planning.

Third Party Activities. The existing regulatory guidance recommends strong control systems to monitor whether the actual practices of third party brokers and correspondent lenders are consistent with the lender's policies and procedures. Generally accepted industry standards and controls for approving and monitoring third party originators currently include licensing reviews, experience requirements, net worth requirements, public records searches, watch and exclude lists, fraud product screening, quality control reviews, due diligence file reviews and contract representation, warranty and remedy provisions. The provisions of the Nontraditional Mortgage Product Guidance and the Subprime Lending Statement could be interpreted to require diligence obligations in excess of these already robust standards.

Since it is virtually impossible to effectively monitor the up-front marketing and disclosure practices of unaffiliated third party originators on a real-time, loan-level basis, it is not reasonable to require financial institutions or secondary market investors to bear the burden of enforcing disclosure requirements and marketing practices of parties over which they have no control. The U.S. residential mortgage industry is dependent on the ability of lenders to easily buy and sell mortgages in the secondary market, and imposing such requirements would have a chilling effect on the secondary market, resulting in a reduction in the overall availability of credit.

Therefore, marketing and disclosure practices should be dictated by modifications to existing federal laws and regulations applicable to all originators and lenders, including brokers, bolstered by federally mandated strict enforcement of uniform broker licensing, reporting, disclosure and training requirements. Brokers should be uniformly obligated to provide written disclosures addressing their obligations to the borrower and their means of compensation. Ultimately, broker enforcement should be the primary obligation of regulators and the legal system, not lenders and investors.

IV. RESPONSES TO QUESTIONS

PREPAYMENT PENALTIES

Q. Should prepayment penalties be restricted? For example, should prepayment penalties that extend beyond the first adjustment period on an ARM be prohibited?

A. When prudently utilized, prepayment fees provide a mutual benefit to both borrower and lender. The benefit to the borrower is a lower initial cost. In return, the lender is assured that the loan will be active long enough to generate a reasonable profit.

Borrowers most likely to benefit from this option are lower-income or first-time homebuyers, who are simultaneously paying a down payment and closing costs. Whether they are purchasing or refinancing, these borrowers typically don't foresee themselves moving or refinancing before the expiration of the prepayment fee period, and want to enjoy the lower cost.

At Chase, we restrict prepayment fees so that they expire at the first adjustment date on a non-prime ARM. We believe that consumers would benefit from other lenders taking the same approach.

Q. Would enhanced disclosure of prepayment penalties help address concerns about abuses?

A. A responsible approach to disclosure is an effective way to ensure borrowers know what they are getting. This includes training the sales force to be aggressively clear about the features of each loan and the consequence of the customer's choice, as well as incorporating prepayment fee information into up-front disclosures and closing documents. To prevent abuses by unscrupulous lenders, this approach should be an industry standard.

At Chase the prepayment fee is disclosed prominently, in writing: (i) during the shopping phase, during which Chase presents the borrower with a plain English, simplified form to assist the borrower in comparing Chase products; (ii) in the up-front RESPA disclosures (a full-page disclosure is dedicated to ensuring the customer knows whether or not their loan features a prepayment option); (iii) on the preliminary TILA disclosure, directly above where the customer signs; (iv) on the final TILA disclosure, also directly above where the customer signs; (v) as a stand-alone attachment to closing instructions; and (vi) as a rider to the ARM note, which the customer signs after review by the closing agent.

Q. How would a prohibition or restriction on prepayment penalties affect consumers and the type and terms of credit offered?

A. A prohibition would make it harder for lenders to make loans and certain borrowers to get loans -- especially low-income and first-time borrowers. One of the greatest hurdles for these borrowers is having enough cash up-front and in the early years of the loan. Prepayment options have become common because they address this genuine consumer need by allowing loan products with lower rates and upfront fees. Without prepayment options, many lenders would stop making some loans – and affected consumers would remain renters.

If there is to be a restriction imposed on prepayment fees, it should be limited to requiring that the prepayment fee expire before the first adjustment.

ESCROW FOR SUBPRIME LOANS

Q. Should escrows for taxes and insurance be required for subprime mortgage loans? If escrows were to be required, should consumers be permitted to "opt out" of escrows?

A. Escrows should be offered one hundred percent of the time to prime and non-prime borrowers, but only "required" of first-time homebuyers with loan to value ratios in excess of eighty percent. The majority of subprime borrowers need and appreciate help in managing their budgets and bill-paying, so it's a customer service to offer escrows—and a potential disadvantage to the borrower not to be given the option. Chase offers non-prime customers this option, and puts their selection in writing in a full-page document included in their up-front disclosures. Experienced mortgage borrowers should have the opportunity to "opt out" being empowered to make their own financial decisions, after being properly educated on their options. Borrowers should also have the option of funding the first or second month's escrow payments into the loan balance. For non-escrowed first lien loans, Chase requires monthly escrow payments if the borrower becomes delinquent.

Q. Should lenders be required to disclose the absence of escrows to consumers and, if so, at what point during the transaction? Should lenders be required to disclose an estimate of the consumer's tax and insurance obligations?

A. Lenders who do not offer the option to escrow taxes and insurance to a non-prime borrower should be required to disclose that up-front, because it's a feature many consumers either assume is available, or are unaware of, and need to learn about before choosing their lender.

At Chase, our non-prime sales team is prompted to discuss escrows and the need to budget for taxes and insurance at two points in the transaction. While taking the customer's application, the loan officer is prompted to offer the option of escrows. Again, at final loan approval, we communicate the estimated amount for taxes and insurance and give the customer the option to escrow. Making this level of disclosure uniform in the industry would certainly benefit all parties.

Chase also includes the following written disclosures: (i) our simplified product comparison, given to applicants while they are shopping for a loan, explains how escrows work; (ii) we estimate hazard and insurance payments in the up-front Good Faith Estimate; (iii) we include a form for the Borrower's Waiver or Election of Escrows in up-front disclosures; (iv) we include an Escrow Account Disclosure Statement, forecasting payments and balances over the next twelve months, in closing documents for borrowers who select that option. Borrowers who escrow should pay lower interest rates than those who waive the option.

Q. How would escrow requirements affect consumers and the type and terms of credit offered?

A. Requiring lenders to offer escrows would positively affect consumers, by providing them an option to assist in budgeting and making the timely payments that are critical to their financial well-being. The type and terms of credit offered by reputable lenders like Chase should not be affected. However, requiring *all* non-prime borrowers to take this option could produce a negative backlash from borrowers knowledgeable and disciplined enough to manage their own cash flow.

STATED INCOME/LOW DOC LOANS

Q. Should stated income or low doc loans be prohibited for certain loans, such as loans to subprime borrowers?

A. No, this would add an unnecessary and significant barrier to homeownership, especially among already under-served classes of borrowers who may not be in traditional, wage-earning jobs. Our mission is to provide home financing to as many borrowers as we responsibly can, and we have found it possible to serve non-prime borrowers who have difficulty documenting part or all of their household income, and to do so prudently.

Q. Should stated income or low doc loans be prohibited for higher-risk loans, for example, for loans with high loan-to-value ratios?

A. In obvious cases of significant risk—such as stated income on a 100% CLTV loan, or stated income on a non-prime, non-owner-occupied property at a high LTV, this might be a reasonable approach. However, it would be a highly complex undertaking to legislate prohibitions based on LTV or other loan or property characteristics. Responsible lenders monitor factors affecting risk and property values on a day-to-day basis across their markets, and have the flexibility to quickly change underwriting guidelines. In order to serve our markets responsively as well as responsibly, we believe these decisions are best managed by the lenders who have the information and financial motivation to do so.

Q. How would a restriction on stated income or low doc loans affect consumers and the type and terms of credit offered?

A. Negatively. While some borrowers choose stated income or low doc loans as a convenience, most self-employed borrowers, or employees who rely heavily on seasonal or side jobs, would be severely affected. Some would be shut out of homeownership completely. Minority and low-to-moderate income borrowers may be disproportionately affected, widening a gap the industry has been working hard to close.

Q. Should lenders be required to disclose to the consumer that a stated income loan is being offered and allow the consumer the option to document income?

A. Yes. Our philosophy at Chase is to be *aggressively* honest and forthright with our borrowers, leaving the final decision in their hands once they've been advised of their options. We think this is the right approach.

UNAFFORDABLE LOANS

Q. Should lenders be required to underwrite all loans based on the fully-indexed rate and fully amortizing payments?

A. Even conservative underwriting should reflect an understanding of borrower needs and behaviors. Many borrowers, especially first-time homebuyers, anticipate either rising incomes or the reduction of other loan obligations by the time their adjustable loan reaches the fully-indexed rate. Others anticipate refinancing their loans before the fully-indexed rate is effective. To mandate an inflexible underwriting standard would make homeownership less affordable, defeating the borrower's purpose for choosing the loan.

It's prudent to qualify short term ARMs with a significant potential for payment shock (where the initial rate is fixed for three years or less, subject to unreasonable payment caps) at the fully-indexed rate at the time of the first adjustment. ARMs fixed for longer than three years can be underwritten at the initial rate, because this likely reflects how long the borrower intends to stay in that loan, and the initial period is long enough to allow the borrower to grow into the payment increase.

Q. Should there be a rebuttable presumption that a loan is unaffordable if the borrower's debt-to-income ratio exceeds 50% at origination?

A. In our experience there are enough exceptions to these criteria to make it anti-consumer to establish it as a hard and fast rule. Seniors in particular may have substantial assets but low or fixed incomes, and the unintended consequences of such a rule could be very negative.

Q. Are there specific disclosures that would help address concerns about unaffordable loans?

A. The most vulnerable borrowers are those who by virtue of age, language barriers or lack of financial sophistication rely on the trust they've placed in an individual loan officer or company. These are the same people least likely to read or scrutinize loan disclosures, or challenge their loan officer. So, while we support clear and effective disclosures, increasing disclosure requirements alone may not be helpful in all cases.

The practice of offering unaffordable loans and other predatory behaviors is best prevented by aggressive enforcement of existing laws and regulations. We need your help to put reputable, heavily-regulated institutional lenders on a level playing field with less scrupulous players, by directing attention and action to the least-regulated segments of our industry. In effect, we need to raise the disclosure standards for unscrupulous lenders to the levels reputable lenders already meet.

Once again Chase appreciates the opportunity to comment. Feel free to contact Marguerite Sheehan, General Counsel - Chase Mortgage at (732) 452-8365 or Denise DesRosiers, Associate General Counsel - Chase Mortgage at (813) 881-2908 with any questions or concerns you may have with respect to the matters addressed in this letter.

Sincerely,

JPMorgan Chase Bank, N.A.

By:______________________________________
Jeffery Polkinghorne, Senior Vice President and Chief Credit Officer
Chase Home Lending Division