MORTGAGE BANKERS ASSOCIATION
Investing in communities

October 11, 2007

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 1-5
Washington, DC 20219

Re: Comments in Response to Proposed Illustrations of Consumer Information for Subprime Mortgage Lending with Request for Comment: Office of the Comptroller of the Currency (OCC) Docket ID OCC-2007-0013, 72 F.R. 45495, August 14, 2007.

Ladies and Gentlemen:

The Mortgage Bankers Association (MBA)[1] greatly appreciates the opportunity to comment on the Notice of Proposed Illustrations of Consumer Information for Subprime Mortgage Lending published by the Office of the Comptroller of the Currency (OCC); the Federal Reserve Board (Board); Federal Deposit Insurance Corporation (FDIC); Office of Thrift Supervision (OTS); and the National Credit Union Administration (NCUA), (collectively "the regulators").[2] We believe that the communication of clear and understandable information to consumers about mortgage products and particular loan terms is vitally important. It gives consumers the ability to make good decisions in light of their own particular circumstances. We applaud the agencies' efforts in this vein and offer comments that we believe would improve the proposed illustrations making them more useful to borrowers.

We would ask that while lenders are not required to use these illustrations, the lending community will heavily rely on and use the final illustrations as part of their own business process. Therefore, we encourage the regulators to seriously consider the recommendations and comments that we offer in response to the proposals as we believe they offer significant value for consumers and lenders alike.

Background

The Statement on Subprime Mortgage Lending published by the regulators on July 10, 2007, addressed lending practices in connection with originating some types of short-term variable rate mortgage products, primarily subprime hybrid adjustable rate mortgages. The Statement

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 500,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 3,000 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web Site: www.mortgagebankers.org.

[2] 72 F.R. 45495 (August 14, 2007).

deals with loans that result in "payment shock" and include one or more of the following characteristics:

- Low initial payment period based on a fixed introductory or teaser rate that expires after a short initial period and then adjusts to a variable index rate plus a margin;
- Very high or no limits on how much payment amount or interest rate may increase ("payment or rate caps") on reset dates;
- Limited or no documentation of borrower's income;
- Product features likely to result in frequent refinancing to maintain affordable monthly payments; and/or
- Substantial prepayment penalties and/or prepayment penalties that extend beyond the initial interest rate period.

The Statement places several conditions on these loans, including; a requirement that they be underwritten to the fully indexed rate; limits on the use of reduced documentation and no-documentation loans unless there are mitigating factors; and requires that consumers get clear and balanced disclosures about the relative benefits and risks of these products. The Statement also requires federally regulated lending institutions to establish quality control systems to assure compliance with these new requirements which will be included as part of the regulators supervisory activities.

The consumer protection portion of the Statement indicates that communications with consumers, including advertisements, oral statements, and promotional materials, "should provide clear and balanced information about the relative benefits and risks of the products."[3] This information should be provided in a timely manner to assist consumers at the shopping stage of the process to select an appropriate loan product. The delivery of such information is intended to supplement the disclosures currently required under the Truth in Lending Act (TILA) and its implementing rules, Regulation Z.

The Notice indicates that the illustrations are not intended to be model forms and lending institutions are not required to use them. Instead, they are provided to demonstrate the type of information that should be provided to consumers pursuant to the Statement. We would request that the regulators underscore and make prominent that these illustrations are examples – and that lenders are able to alter them according to the product and terms offered.

The Notice specifically invites comment on all aspects of the Illustrations including whether the Illustrations, as proposed, would be useful in promoting consumer understanding of the risks and material terms of certain ARM products, as described in the Statement, or whether changes should be made to them. The regulators also seek comment on whether the information in the proposed illustrations is set forth in a clear manner and format, whether these illustrations should be adopted by the regulators, and whether there are additional illustrations relating to certain ARM products that would be useful to consumers and lending institutions.

[3] 72 F.R. 37574 (July 10, 2007).

Proposed Subprime Illustration

MBA supports the proposed illustrations provided by the regulators and we offer the following comments to improve the communication of information to consumers about short-term subprime ARMs. The Notice proposes two Illustrations for comment:

(1) Illustration 1 entitled "Important Facts About Your Adjustable Rate Mortgage" addresses, in brief terms, the initial interest rate of a hybrid ARM product, taxes and insurance, prepayment penalties, balloon payments, and the costs of reduced documentation or state income loans.

(2) Illustration 2 entitled "Sample Mortgage Comparison" is a chart that compares the payments over the life of a fixed rate product versus a "2/28" hybrid ARM.

Illustration 1

The first illustration is a narrative explanation of some key features of certain ARM loans. The following are technical recommendations that, in our view, reflect market realities and would improve the conveyance of information to consumers:

- In the second paragraph, the second sentence discusses changes to a borrowers interest rate and states, "Instead, it changes over time according to a formula – typically, a base interest rate (index) plus a certain percent (margin) (for example, the Prime Rate plus 3 percent.)" Lenders do not use "Prime Rate" as an index. They use close to a dozen indices including U.S. Treasury rates or the London Interbank Offered Rate (LIBOR). We would recommend that the illustration reflect this market reality.
- Illustration 1 is intended to present consumers with information about a particular type of loan in a timely manner – preferably as early as possible during the stage of shopping for a loan. Loan features are not final when consumers are shopping for mortgages. In light of this, the subject headers following the arrow bullet points on Illustration 1 would be more accurate if it indicated the possibility that a loan "may" have a particular feature rather than communicate that it "will" have a particular feature. We recommend the following changes:
    - "Your loan ~~will~~ **may** have a reduced initial interest rate."
    - "Your monthly payment ~~will~~ **may** not include an amount to cover taxes and insurance."
    - "You ~~will~~ **may** be required to pay a prepayment penalty if you..."
    - "Your loan ~~will~~ **may** have a balloon payment."
    - "Your loan ~~will~~ **may** have a higher price because of reduced documentation."
- In the interest of clarity, in the paragraph explaining the payment of taxes and insurance, a final sentence should be added: "You are responsible for the payment of taxes and insurance regardless whether your loan includes an escrow."
- The bullet point describing prepayment penalties would provide greater consumer understanding with some modest clarifications and a pronouncement of the benefit a prepayment penalty can offer a consumer. The following paragraph reflects our comments including strike throughs and our recommended language in italics:

You ~~will~~ *may* be required to pay a prepayment penalty if you pay off your loan *early* ~~more than sixty days before the initial interest rate adjustment~~. The amount of the penalty will be a percentage of the outstanding balance of the loan *or it may require the payment of a certain number of months advance interest.* Some ARMs require ~~you to pay a large~~ *a* prepayment penalty if you sell your home or refinance during the first few years of the loan. *In exchange for a potential* prepayment penalty*, a consumer can obtain the benefit of lower monthly costs; however, a prepayment penalty* can make it difficult, or very expensive, to sell your home or refinance – which you may need to do if your interest rate, and therefore your payment, is about to increase significantly.

Illustration 2

While the chart, "Sample Mortgage Comparison," provides a flexible example of monthly payments, two improvements would update the illustration so that it suits the current market in which consumers are shopping. First – and most importantly – there ought to be a clear statement indicating that these figures represent a hypothetical example intended to educate the potential borrower at an early stage about the payment adjustment that could result from a short-term subprime ARM. Without such a statement the chart could mislead a viewer into believing that the numbers used and indicated payment adjustment reflect market reality.

Second, this illustration should be based on the actual index used by the lender and not "Prime Rate" – as referenced in the first illustration. As noted earlier, lenders use close to a dozen different indices such as the U.S. Treasury rate or LIBOR.

General Remarks about Mortgage Disclosures

MBA supports a comprehensive approach to improving and streamlining the mortgage disclosure process in an effort to provide clear and balanced information to borrowers about the loan products and loan terms that they are shopping for or have been offered. Instead of a simple disclosure, consumers today confront a pile of disclosures when they apply for and close on a mortgage. Sadly, every new layer of disclosures simply increases the likelihood that the consumer will merely initial all of them without even a cursory reading. For this reason, disclosures do not need to be added; they need to be combined, streamlined and made much more user friendly.

MBA initiated an effort called "Project Clarity" to communicate the most important elements of a mortgage to a consumer. Project Clarity resulted in two tools - "The Simple Facts", which is a plain language disclosure of the most important terms of a mortgage, and "The Simple Calculator" to help consumers compute the cost of a mortgage. The Simple Facts and the Simple Calculator are the result months of focus groups and testing. These tools are available for consumers on MBA's Home Loan Learning Center Web site (www.HomeLoanLearningCenter.com).

Providing better information – not more – through improved financial literacy programs and improved and simplified disclosures would significantly improve consumers' understanding of the financial contracts that they are considering. The Federal Trade Commission recently concluded, after reviewing studies on mortgage disclosures, that "[c]urrent mortgage disclosures fail to convey key mortgage costs to many consumers." These economists also concluded that "[i]t is possible to design better disclosures that significantly improve consumer recognition of mortgage costs."[4] MBA stands ready to assist policymakers in an effort to streamline and improve existing mortgage disclosures.

Conclusion

Again, MBA greatly appreciates the opportunity to comment on these illustrations. We fully support the communication of important information about mortgage products and loan terms and we commend the regulators efforts. If you have any questions or concerns, please do not hesitate to contact Mary Jo Sullivan at msullivan@mortgagebankers.org or (202) 557-2859. MBA looks forward to continuing to work with the regulators on these issues.

Sincerely,

John M. Robbins, CMB
Chairman

[4] James M. Lacko & Janis K. Pappalardo, Bureau of Economics, Federal Trade Commission, *Information Regulation is Tricky: Lessons from Mortgage Disclosure Research*, presentation before the Behavioral Economics and Consumer Conference, Federal Trade Commission, Washington, D.C. (April 20, 2007); *see also* James M. Lacko & Janis K. Pappalardo, *The Effect of Mortgage Broker Compensation Disclosures on Consumers and Competition: A Controlled Experiment*, Federal Trade Commission Bureau of Economics Staff Report (2004), available at http://www.ftc.gov/os/2004/01/0301/030123mortgagefullrpt.pdf.