From: Bethany Sanchez <bethany_sanchez@hotmail.com> on 04/08/2008 03:00:03 PM

Subject: Regulation Z

(comments sent via email, hard copy to follow in snail mail)

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

RE: Regulation Z, Docket No. R-1305

Dear Secretary Johnson:

I am writing today on behalf of the Metropolitan Milwaukee Fair Housing Council (MMFHC), to comment on the proposed changes to Regulation Z - changes that are intended to end unfair and deceptive practices on high-cost loans.. First, I would like to provide some information on our work, so that you have a feel for the perspective that MMFHC brings to the issue.

In late 2001, MMFHC created Strategies to Overcome Predatory Practices (STOPP), an initiative that utilizes a coalition of community-based organizations, housing industry representatives and government to identify and eliminate discriminatory, fraudulent, unfair, and predatory lending practices throughout Milwaukee County. MMFHC staff members take calls from borrowers and potential borrowers on a special STOPP hotline, review loan documents and provide input and advice. Borrowers facing foreclosure receive information on the process and timing of foreclosure, and the options they have for avoiding the loss of their home. Depending on the borrowers' circumstances, we may also assist the borrower by helping to negotiate with the existing lender. When predatory loans are uncovered, we coordinate a plan, working in cooperation with other STOPP partners to help the client clean up the borrower's credit, pursue legal options if warranted, and obtain a new affordable home loan, suitable for their circumstances.

STOPP also coordinates: a variety of outreach and education activities presenting borrowers and community groups with information about unfair and predatory loan practices, a workgroup seeking ways to refinance troublesome loans, research activities documenting lending and foreclosure problems in Milwaukee County, and a legislative workgroup that is currently providing the Wisconsin State Legislature with technical assistance on proposed legislation prohibiting foreclosure "rescue" scams.

We believe that the Federal Reserve Board has taken an important step in proposing changes to its Regulation Z. The nation faces a foreclosure crisis in large part because risky lending was not constrained, due to a lack of consumer protections and safety and soundness standards. The proposed changes are a substantial move in the right direction.

In Milwaukee, high-cost lending is heavily concentrated in communities of color. But it is not limited to those neighborhoods. It has even become prevalent in middle-income neighborhoods as borrowers have stretched their incomes to buy larger homes than they could afford. Foreclosures and distress have become widespread, with all levels of government now scrambling to address the interconnected issues and repercussions from the toxic, inappropriate loans people received, and the resulting foreclosures.

While the Federal Reserve's proposal is critical and overdue, it has significant openings and exceptions in its major provisions dealing with unfair lending practices. The proposal has

commendable aspects, but these open areas could render the provisions unenforceable and/or relatively weak. We urge the Federal Reserve to address these areas and ensure that there are no opportunities to circumvent its major provisions.

Our comments on specific aspects of the proposal include the following:

Ability-to-Repay: We support the proposal that a lender's ability-to-repay analysis for high-cost and very high cost loans must consider a fully-amortizing payment that includes property taxes and insurance. In addition, we support the proposed underwriting based on the fully-indexed rate and the maximum possible rate as specified in loan contracts for step-rate adjustable rate mortgages (ARMs) with an initial teaser rate. The proposed residual income analysis is also vital since lenders must make sure that borrowers truly have enough income left over after monthly debt payments to afford other basic necessities. The proposed standards will curb the practice of qualifying borrowers on the initial, teaser rate – a practice that has contributed to "payment shock" and borrowers becoming delinquent after the loan's rate increases dramatically from the initial rate.

Unfortunately, other aspects of the proposed ability-to-repay standard threaten to undermine protections against unfair and deceptive lending. For example, the proposal requires lenders to verify borrowers' income with tax documents and pay stubs. However, the proposal then allows lenders to avoid documentation requirements if they can demonstrate that assumed borrower income and asset levels were not significantly greater than levels the lender could have documented when approving the borrower's loan application. This confusing exception essentially permits the practice of limited documented lending to continue. In addition, the proposed rule allows lenders to assure that borrowers can repay loans during the first seven years of a loan's life. Many borrowers of limited means will not refinance after seven years, meaning this proposed underwriting standard will not provide them with sufficient protections. Finally, and importantly, the ability-to-repay standard requires borrowers suing lenders to prove that the lenders exhibited a pattern and practice of making unaffordable loans. This is a very difficult standard for borrowers of few resources to prove. Existing state law does not raise the bar this high. The Federal Reserve should at least allow individual lawsuits under a standard that is not so difficult to prove. It would seem that a regulation that allows individual lawsuits, if not class actions, should not establish such an onerous standard to defend oneself against abusive lending.

Escrows Required: The proposal recognizes the importance of requiring escrows on high-cost and very-high cost loans. Yet, it permits a lender to allow a borrower to opt-out of escrow requirements after twelve months. Borrowers not familiar with the loan process can be swayed to opt-out of escrow requirements and then face unaffordable expenses that they were not advised to anticipate. The proposal should not allow for the elimination of escrow requirements on high-cost and very-high cost loans.

Prepayment Penalties: The proposal to ban prepayment penalties after 5 years is too long of a time period for high-cost and very-high cost loans. Some borrowers may need to refinance before that time to escape unaffordable loans. Others may have significantly improved their credit scores, and should not be penalized by paying thousands of dollars in prepayment penalties to refinance out of high-cost loans. Major lending institutions have voluntarily adopted a three year limit. We urge the Federal Reserve to follow these best practices and set a limit of between two to three years. The prepayment penalty should also be limited to a reasonable dollar amount so that the penalty does not pose a barrier preventing a refinance into a lower cost loan.

In addition, we agree with the Federal Reserve that prepayment penalties must cease before the initial rate expires on an ARM loan. But we urge the Federal Reserve to require prepayment penalties to cease 90 days before the expiration of the initial rate, not 60 days as proposed, so that borrowers truly have enough time to shop for another loan.

Yield Spread Premiums: Yield spread premiums (YSPs) must be banned on high-cost and very-high cost loans instead of the proposed improvements in disclosures of YSPs. When YSPs are used, interest rates on a loan are raised beyond the rate a borrower qualifies for so that brokers can be paid. In exchange for the higher interest rates, YSPs are supposed to significantly lower broker fees and other fees. However, our experience here in Milwaukee, and the experience of foreclosure prevention counselors around the country suggests that YSPs on subprime loans are double-dipping opportunities for brokers and lenders: higher interest rates and usurious fees are imposed. The subprime market is too complicated for borrowers unfamiliar with the loan process to be assisted in a meaningful way by enhanced disclosures of YSPs.

Protections for All Loans : We support the proposed protections against appraisal fraud, servicing abuses, and deceptive advertising. We also support the proposed requirement that good faith estimates (GFE) of loan costs for refinance and other non-home purchase loans be supplied to borrowers before payment of application fees. After payment of application fees, borrowers are much less likely to use the GFE to shop for the best deal.

The Federal Reserve's proposals for these provisions are not comprehensive enough. For example, in the area of servicing, the Federal Reserve needs to require reasonable loss mitigation efforts before foreclosure proceedings are commenced. Protections against appraisal fraud must require a new appraisal and an adjusted loan amount in cases when the original appraisal was inflated.

Non-Traditional Prime Loans not Covered: MMFHC is concerned that the Federal Reserve has proposed protections regarding ability-to-repay, escrows, and prepayment penalties for high-cost loans only, and has not proposed these protections for exotic prime loans such as option ARM loans that have proven to be problematic. Since the Federal Reserve has already agreed to ability-to-repay standards for non-traditional loans in guidance that applies to banks, it would be inconsistent to not apply these protections for non-traditional loans made by all types of lenders. This uneven regulation would allow mortgage companies and other non-banks to continue to engage in dangerous non-traditional lending while banks would be prohibited from doing so. It allows non-banks to compete through unscrupulous practices, to the detriment of borrowers and responsible banks.

Liability for Secondary Market: Aside for violations including very high-cost loans, the secondary market's liability is quite limited. For all other loans, the secondary market is held liable only in cases of violations of certain disclosure requirements. Since most subprime loans are sold to investors, the limited liability for investors provides no effective redress for borrowers. At the least, the Federal Reserve should broaden liability and allow individual borrowers to seek redress, if not class action lawsuits.

Conclusion

We join with our colleagues across the country, including the other members of the National Community Reinvestment Coalition, in urging the Federal Reserve to significantly strengthen and then implement its proposal. Inadequate consumer protection regulation has significantly contributed to discrimination and fraud, leading to the foreclosure crisis and the current economic uncertainty. Our comments address the role we feel is necessary for

the Federal Reserve to play. At the same time, we acknowledge that Congress needs to pass a strong anti-predatory lending bill covering all parts of the lending industry.

Thank you for this opportunity to provide comments on this important matter.

Sincerely,

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cc: National Community Reinvestment Coalition