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Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Truth in Lending; Docket No. R-1305
73 FR 1672 (January 9, 2008)

Dear Ms. Johnson,

Thank you for the opportunity to comment on the Federal Reserve System's (hereinafter the "Federal Reserve") proposal to amend Regulation Z. The New York Bankers Association (NYBA) commends the Federal Reserve for its efforts to offer further protections to consumers against predatory lending practices in the mortgage market and we support many of the proposed amendments. Nevertheless, we believe that changes are necessary - most particularly to the proposed definition of higher-priced loans - to ensure that the new provisions are not so overly broad or restrictive as to impede unnecessarily the flow of credit to worthy borrowers in the prime and subprime mortgage markets. Our specific comments are set forth below. NYBA is comprised of the commercial banks and thrift institutions that do business in New York State. Our members employ more than 300,000 New Yorkers and have assets in excess of $9 trillion.

The IMPORTANCE OF UNIFORM, NATIONWIDE STANDARDS

As a general comment, NYBA believes that all elements of the mortgage lending business should be subject to the same lending requirements and regulatory enforcement as federally insured depository institutions are today. As all the federal regulators have testified before Congress, the vast majority of the abusive mortgage origination practices that helped lead to today's mortgage crisis were not committed by members of the highly regulated banking community, but rather by non-bank lenders, brokers and mortgage servicers who are not now subject to the same regulatory scrutiny and regimen as depository institutions. Consumer protection cannot be complete in the mortgage market until and unless non-bank financial firms are regulated and are subject to the same enforcement standards as federally regulated institutions. We also believe that, as today's mortgage market transcends local and state boundaries, nationwide, uniform standards are necessary to avoid a confusing patchwork of conflicting law and regulation across the country, and to ensure strong, consistent protection to all borrowers, lenders and investors.

HIGHER PRICED LOANS

NYBA believes that many of the proposed amendments to Regulation Z can offer important additional protections for subprime borrowers and help restore confidence in the mortgage and credit markets. However, we are concerned that the proposed threshold definition of a "higher-priced" loan would unintentionally and unnecessarily capture a substantial portion of loans in the prime and Alt-A markets, including many prime adjustable rate mortgages, jumbo loans, small mortgage loans, zero upfront closing cost loans and home equity loans. We are concerned that the proposal would therefore expose banks to significant new restrictions and legal liability which can only result in additional costs, fewer meaningful product offerings, and reduced access to credit for all lenders and borrowers - with little or no offsetting benefit.

Higher-Priced Loan Threshold: The proposal defines a higher-priced loan as a consumer residential mortgage loan with an APR greater than three percentage points over comparable Treasury securities (five percentage points over Treasury securities for subordinate liens). We believe that this definition is far too expansive, and would have the unintended effect of converting a significant percentage of today's prime and Alt-A market into "higher-priced" loans. Given the severity of damages for violations of requirements for higher-priced loans contained in this proposal, coupled with banks' concerns that offering "higher-priced" loans will create reputational risk, the overly broad definition of such loans could have a dramatic impact on the availability and cost of credit to consumers seeking mortgage loans.

We believe that the definition of "higher priced loan" is inappropriately broad, both because of the threshold's link to the yield on Treasury securities and because the proposed spread is inappropriately low. Due to the recent disruptions in the historical correlation between Treasury securities and mortgage rates (caused by, among other things, the flight to quality by domestic and international investors and the resulting decrease in yields, and the evolution of the secondary market whereby capital markets now largely drive mortgage rates) use of the yield on comparable Treasury securities is no longer an appropriate measure for mortgage rates. We believe, instead, that the definition of a higher-priced loan should be based on an index that consistently tracks mortgage rates and therefore is more relevant to pricing in today's mortgage market.

One possible alternative would be to measure a higher-priced loan as a mortgage that has an APR that exceeds a specified threshold over a rate published by a government sponsored enterprise (GSE), such as the Freddie Mac Weekly Mortgage Market Survey, as is included in the Federal Reserve's H.15 schedule. Should such an alternative index be adopted, a spread close to the proposed three and five percentage points might be considered appropriate – but only if it took into account the pricing differences that result from loan terms and other risk parameters of low-risk, benchmark mortgages.

If the Federal Reserve elects to continue to use Treasury securities as the benchmark for identifying higher-priced loans, it is imperative that the spread over the comparable Treasury security be increased from its current 3% level, to offset the variations that can occur between Treasuries and mortgage rates. As stated earlier, if the spread is not increased, it would capture many prime mortgages due to the changes in the yield curve as well as other factors that affect the pricing of a loan, including, but not limited to the loan-to-value ratio, the borrower's credit score, and secondary market surcharges. Without comprehensive industry data, we are unable to determine with certainty what the appropriate spread over Treasuries should be although we have heard anecdotally that a spread of five percentage points over Treasury securities for first lien loans and seven percentage points for subordinate liens might be workable.

Should Treasury securities continue to be the benchmark, we urge the Federal Reserve to study the data that it receives during this comment period as well as relevant HMDA data in order to develop a spread that: 1) ensures that no prime and fewer Alt-A loans are captured in the higher-priced category; 2) allows borrowers with acceptable risk features to continue to have access to prime lending without triggering features intended for subprime borrowers; and 3) provides sufficient flexibility to address the lack of correlation between Treasuries and the mortgage market.

We are also concerned that the proposal uses a different approach than in Regulation C for matching the comparable Treasury securities to particular loan terms. Regulation C compares the APR on a loan to the yield on Treasury securities having a period of maturity comparable to the maturity of the loan, while the proposal would match loans to Treasuries based on whether the loan is adjustable or fixed, the term of the loan, and the length of any initial fixed-rate period if the loan is an adjustable-rate mortgage. We believe that creating an additional matching standard would only create confusion and further increase the complexities of compliance, and therefore urge that a separate methodology not be mandated in the final rule.

Specific Requirements Pertaining to Higher Priced Loans

The proposal includes a number of additional consumer protections, which are of concern in their present form, particularly if the thresholds in the final rule are not altered.

Repayment Ability: The amendments would prohibit lenders from engaging in a pattern or practice of making higher-priced mortgage loans without regard to a consumer's repayment ability, including the consumer's current and reasonably expected income, current and reasonably expected obligations, employment, and assets other than the collateral. Lenders would be required to document a consumer's ability to repay the loan. While we agree that evaluating a consumer's repayment ability is a key principle of safe and sound lending, we are concerned that the proposed rule effectively mandates industry-wide underwriting standards, rather than permitting financial institutions to determine - as they do now - underwriting criteria that reflect their institutions' individual levels of risk tolerance. If the Federal Reserve moves forward with a final rule, we request that the rule and its accompanying commentary provide clear guidance regarding what an institution must do in order to "consider" income, debt, ordinary living expenses, and residual income. In addition, the Federal Reserve should clearly define the meaning of these underwriting terms. These clarifications are essential in order to avoid ambiguities and the potential for disparate treatment or disparate impact on applicants in protected groups.

Pattern or Practice Standard: The proposal creates a rebuttable presumption that a lender failed to consider a borrower's repayment ability if the lender engages in a "pattern or practice" of failing to verify and document repayment ability. We believe that this is an appropriate approach for determining an originator's civil liability for failure to consider a borrower's ability to repay. However, we would urge the Federal Reserve to clarify the "pattern or practice" standard in the underwriting context, so that the same standard would be applied in all jurisdictions and the level of untoward litigation for alleged violations would be minimized.

In this regard, for example, clarification is needed to ensure that violations that involve a small percentage of an institution's total lending activity are not determined to be a "pattern or practice". Additionally, it should be made clear that "pattern or practice" is not automatically deemed to exist where a lender relies on a written or unwritten lending policy or upon underwriting software for its mortgage loans. Indeed, banks are required to use the automated underwriting systems Desktop Underwriter or Loan Prospector when making loans that will be sold to the GSEs. Clearly, they should not be held liable if loans originated using these systems are found to constitute a "pattern or practice" of failing to consider a borrower's ability to repay. We respectfully urge the Federal Reserve, in its final rule, to clarify that lenders that use automated underwriting systems that are developed by a bank or a bank aggregator are not considered to engage in a "pattern or practice" for purposes of the regulation as long as the creditor is regularly examined by a Federal regulatory agency for compliance with fair lending laws and regulations.

Prepayment Penalties: Prepayment penalty provisions that are clearly disclosed can benefit both borrowers and lenders, as consumers may choose to accept such a penalty in return for a lower interest rate or lower closing costs, while lenders benefit from increased predictability of loan duration. Therefore, NYBA believes that this loan option should be preserved. Many of the benefits from the use of prepayment penalties could be obtained, and the abuses associated with these clauses could be avoided, if prepayment penalties were not permitted to extend beyond 60 days before the first payment reset in cases in which the payment reset is substantial (i.e., greater than 15% compared to the original payment).

Escrow: The proposed rule would require lenders to establish an escrow account for higher-priced mortgage loans that are secured by a first lien. Creditors would be permitted, but not required, to allow borrowers to opt out of the escrow account twelve months after the consummation of the loan. We agree that lenders should consider the ability of a borrower to pay taxes and insurance when evaluating creditworthiness. Moreover, homebuyers need to be adequately informed about the costs of homeownership, including the obligation to pay property taxes and premiums for homeowners insurance. However, many financial institutions have elected not to establish departments within their banks to collect and pay taxes and insurance premiums on behalf of their borrowers. The proposed rule could therefore impose significant new costs and an ongoing compliance burden, which would undoubtedly result in more costs to consumers and less access to credit for worthy borrowers. We respectfully urge the Federal Reserve to adopt instead a disclosure alternative to the proposed escrow requirement which would mandate a disclosure of estimated taxes and insurance based on the previous year's assessment. Should the Federal Reserve decide to include an escrow requirement in the final rule, we ask that financial institutions be given eighteen months at least to implement the escrow system.

PROVISIONS APPLICABLE TO ALL MORTGAGE LOANS

For all mortgage loans, the proposed rules would regulate the compensation of mortgage brokers, prohibit creditors and brokers from coercing a real estate appraiser to misrepresent a home's value, and would establish rules to prevent servicers from engaging in unfair fee and billing practices. Subject to the suggested changes set forth below, NYBA supports these disclosure, appraisal, and servicing practices, which are, in fact, already standard practice today for most insured depository institutions.

Mortgage Broker Compensation. The proposal seeks to increase the transparency of a mortgage broker's compensation by requiring that: (i) a mortgage broker not be paid a yield spread premium unless the consumer agrees in advance to the dollar amount that the broker will receive as compensation; and (ii) the broker and the consumer enter the agreement before the consumer pays a fee to any person or submits a loan application. This rule would apply even if all or part of the broker's compensation is paid directly by the creditor. While we believe this additional disclosure mechanism would increase transparency, we are concerned that, as drafted, financial institutions – through no fault of their own - could be liable for violating this provision if such an agreement were not signed in a timely manner. We therefore request that, should this proposal be included in a final rule, the rule 1) specify that creditors may rely on the face of the broker compensation agreement for purposes of complying with the proposal; 2) impose a direct obligation on the mortgage broker to provide the broker disclosure/fee agreement; and 3) expressly prohibit mortgage brokers from accepting any fees or the consumer's loan application until the consumer signs the fee agreement. These requirements should be in addition to the limitations that would apply to creditors.

As stated above, NYBA strongly supports meaningful disclosure and is in favor of increased transparency regarding broker compensation. However, we believe that any new rules regarding broker compensation should be adopted in conjunction with the Department of Housing and Urban Development's (HUD) initiative that is underway to reform the disclosures for broker compensation under the Real Estate Settlement Procedures Act (RESPA). HUD's proposal, also recently published for public comment, differs from the Federal Reserve proposal as to the timing, form and content of the disclosures. It would be costly and confusing to financial institutions and consumers alike and would make bank compliance extremely difficult if there existed two varying rules dealing with the same subject matter. We therefore strongly urge the Federal Reserve and HUD to issue one set of coordinated regulations and disclosures.

Appraisals. NYBA strongly supports the provisions in this proposal that would prohibit creditors and mortgage brokers from coercing appraisers to misrepresent the value of a consumer's dwelling. The new provisions are consistent with existing regulations that already apply to federally insured depository institutions, and we believe it only appropriate that all mortgage market participants, including mortgage brokers, be expressly prohibited from improperly influencing an appraisal. We are concerned, however, that as currently drafted, Section 226.36(b)(2) would unfairly hold creditors liable for the actions of independent mortgage brokers whom they do not control. This provision - which prohibits a lender from extending credit if it knows or "has reason to know" that a broker improperly influenced an appraiser – is of particular concern as it is overly broad and ambiguous, and yet would make financial institutions vulnerable to potentially significant liability for violation of its terms (including recovery by consumers of actual damages, statutory damages, court costs, and attorney fees). We believe that it would be far more appropriate if the "reason to know" standard was replaced by an "actual knowledge" standard, whereby a lender would be prohibited from making a loan if it had actual knowledge that the appraisal was inflated.

Servicing. For the most part, NYBA supports the proposed servicing standards set forth in this proposal, as they would require all servicers to adhere to industry standards that are consistent with the business practices already utilized in depository institutions. However, we are concerned that the new restrictions or requirements for mortgage servicing would be adopted under TILA §129(l)(2), which contemplates the assessment of statutory damages, finance charges and fees paid on the loan, and attorney's fees for violations - unless the creditor demonstrates that the failure to comply "is not material". We believe that these potential penalties are not proportionate to the harm that the seeming violations would cause to the consumer, and therefore respectfully request that the Federal Reserve specify that a violation of the servicing requirements in proposed §226.36(d) are not "material" for purposes of the relevant civil liability provisions.

Additionally we request that several other clarifications be made to the servicing provisions of the proposal. We believe that the rule that requires that consumers receive a fee schedule within a reasonable time after requesting information about a servicer's fees should be crafted to provide servicers with sufficient flexibility to provide information to the best of the servicer's ability, recognizing that some fees will be difficult to know with certainty. Additionally, the proposed commentary states that fees imposed by the servicer include third party fees that the servicer passes on to the consumer. Charges by third parties differ across the country, thereby making it difficult to provide precise information to a specific consumer. We therefore respectfully request that servicers be required to disclose only standard fees or common fees such as non-sufficient funds fees or duplicate statement fees. Finally, we ask that the proposed rule be clarified to specifically permit servicers to continue the current common practice of crediting mortgage payments back to the date of receipt.

ADVERTISING

We request that the Federal Reserve conduct consumer testing in order to study whether the proposed extensive advertising disclosures contained in this proposal would be useful to consumers or whether such detailed information would be more helpful if it were provided in other disclosure contexts.

CONCLUSION

NYBA supports the extension of uniform regulatory oversight to nonbank lenders, mortgage brokers and servicers. However, we are concerned that the proposed thresholds in this proposal for defining loans as "higher-priced" would enmesh many prime and Alt-A loans within the category's restrictions. This is of great concern to bankers because of the additional compliance costs, the significant increase in potential liability exposure, and the risk to their institutions' reputations. These negative effects on financial institutions will inevitably lead to increased costs to consumers, fewer choices in mortgage products, and ultimately to a reduction in credit availability for many consumers. We urge, therefore, that these thresholds be revisited to include only those loans that can legitimately be deemed "higher-priced".

We also urge the Federal Reserve to ensure that the final broker compensation, appraisal and servicing provisions do not hold regulated depository institutions responsible for the acts of third parties and do not subject well-established businesses processes by responsible mortgage lenders to new and inappropriate levels of potential liability. With these changes, the rules can provide additional customer protections, while ensuring continued availability of affordable mortgage credit to all consumers.

Thank you for the opportunity to comment on this important matter. If you have any questions, please do not hesitate to call me at (212) 297-1699.

Sincerely,

Michael P. Smith