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April 7, 2008

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

Subject: Docket No. R-1305  
Comments regarding 12 CFR Part 226  
Truth in Lending; Proposed Rule

Dear Ms. Johnson:

Thank you for the opportunity to comment on the Proposed Rule of the Federal Reserve System to amend Regulation Z, as set forth in the Federal Register on January 9, 2006.

The National NeighborWorks® Association (NNA) is the national trade association of “NeighborWorks” organizations. Our membership includes over 170 nonprofit organizations, serving communities across the United States -- in 47 states, and the Commonwealth of Puerto Rico. NeighborWorks organizations operate in our nation’s largest cities and in some of its smallest rural communities.

Local NeighborWorks organizations provide a wide variety of services that reflect the needs of their neighborhoods and communities, and over the years, the NeighborWorks Network has provided homeownership counseling to more than 500,000 families, and assisted nearly 150,000 families of modest means to become homeowners. NeighborWorks organizations also own and manage more than 70,000 units of affordable rental housing. In FY 2007 alone, the NeighborWorks network generated about \$4 billion in direct reinvestment in distressed communities across the nation.

Our members have a 30-year history of facilitating lending to non-conventional borrowers – including lower income families, borrowers with impaired credit and others who would not normally qualify for a conventional mortgage.

By providing quality pre-purchase homeownership counseling, financial fitness training and working with borrowers to improve their credit rating; improve their budgeting; and commit to a savings plan (including Individual Development Accounts and other vehicles), local NeighborWorks organizations are able to prepare foreclosure-resistant

borrowers who qualify for reasonably priced traditional mortgage loans and achieve sustainable homeownership.

From our experience, we know that the best defense against mortgage delinquency and foreclosure is objective education and counseling before the borrower begins shopping for a home and selecting a mortgage product – or refinancing their home. The best home buyer counseling is provided through objective, well-trained non-profit agencies (including local NeighborWorks organizations and other HUD-approved housing counseling agencies) that put the consumers’ and the communities’ interest first. We also know that homeowners’ odds of success are increased even further when they have access to post-purchase counseling and homeowner education.

Neighborhood Reinvestment (d/b/a NeighborWorks America), the national intermediary that supports local NeighborWorks organizations, has been closely tracking the loan performance of the many low-income families assisted by NeighborWorks organizations over the years. *These loans continue to perform significantly better than subprime loans.* We have not seen any significant up-tick in defaults or foreclosures among NeighborWorks-assisted families. In fact, a comparison of the loan performance of a sample of borrowers counseled by NeighborWorks organizations indicates that their loans are:

- 10 times less likely to go into foreclosure than subprime borrowers;
- Nearly 4 times less likely to go into foreclosure than FHA borrowers; and
- Slightly less likely to go into foreclosure than Prime borrowers.

**Comments Regarding Proposed Rule:**

NNA is supportive of the efforts being taken by the Federal Reserve System through this Proposed Rule, to increase the level of disclosure and transparency in the mortgage industry and protect consumers from unfair, abusive, or deceptive lending and servicing practices.

However, given the current degree of problems in the mortgage industry, as evidenced by the rising foreclosure rate and its impact on the broader economy, we believe that certain additional steps are needed. We have set forth our comments below:

**Definition of “higher-priced mortgage”**

NNA is supportive of the proposed definition. The proposed APR threshold for a loan at three percentage points above the comparable Treasury security, or five percentage points in the case of a subordinate-lien loan is clear and we believe it will work well.

**Proposed prohibition to engaging in a pattern or practice of extending credit to a consumer without regard to the consumer’s repayment ability**

NNA is in strong support of this proposal. The practice of providing a loan based on the consumer’s collateral alone, without regard to the borrower’s ability to repay, is clearly a contributing factor to the current mortgage foreclosure crisis. Whether or not the lender is able to recoup their investment from the consumer’s collateral, when these loans fail, it

is not only the individual borrower who suffers. We believe the Federal Reserve has a responsibility to protect the broader community and the capital markets from the negative impacts of foreclosure.

We are however concerned that, as currently written, the new rule would only prohibit a lender from “*engaging in a pattern or practice*” of making mortgage loans based on the value of a consumer’s collateral without regard to the consumer’s ability to repay. This language (i.e. “*engaging in a pattern or practice*”) would establish a legal standard that would require a borrower seeking redress to demonstrate not only that the lender made a loan that was clearly unaffordable to him or her, but to also prove that the lender engaged in a “pattern or practice” with regard to other borrowers. Given that individual borrowers (or their attorneys) cannot easily obtain empiric evidence regarding other loan transactions, this would be an extremely difficult standard to prove, even when there have been flagrant violations. We also believe the use of the phrase “*engaging in a pattern or practice*” would create a lack of clarity for lenders (i.e. As to whether an individual decision they are making is appropriate, or whether it would be seen in the context of a “*pattern or practice*”.) We believe this should be set forth as a more straightforward prohibition on extending credit without consideration of the borrower’s ability to repay.

We are also concerned that the proposed prohibition limits the standard to subprime loans only, and does not include other nontraditional loans, such as “Payment Option Adjustable Rate Mortgages” and other Alt-A products. We believe this regulation should be expanded to cover all non-traditional mortgages.

### **Verification of Income and Assets Relied on**

The Federal Reserve should prohibit so-called “stated income” loans. Clearly, if the Federal Reserve implements the proposed “consumer’s repayment ability” provision, a verification of income becomes an absolutely necessary component of any meaningful standard. Without adequate income verification, any other underwriting and/or loan approval process is meaningless. There is clear evidence that “stated income” loans result in a frequent overstatement of income and therefore ability to repay, thereby directly contributing to the current foreclosure crisis.

We are again concerned that the Proposed Rule would require income verification on subprime loans, but would not require it for other nontraditional loans. We believe this standard should be extended to cover other nontraditional loans.

### **Prepayment Penalties**

While the proposed limitation on prepayment penalties will help, we respectfully ask that the Federal Reserve consider a ban on all prepayment penalties. Prepayment penalties essentially trap borrowers in bad loans, when they would otherwise have access to more affordable refinance products. They are disproportionately associated with loans to people of color, and to families with modest incomes, and loans with prepayment penalties have a significantly higher incidence of foreclosure than other loans. Compounding the problem is the lack of transparency around prepayment penalties. Most people don’t even realize that they have a prepayment penalty provision built into

their mortgage, until they try to refinance or pay-off the mortgage – and then realize they are “trapped”. And, it is not clear that borrowers receive any benefit from prepayment penalties.

### **Requirement to Escrow for Taxes and Insurance**

NNA is supportive of the Board’s proposal to prohibit a creditor from making higher-priced loans without establishing an escrow account for property taxes and homeowners insurance. Foreclosure counselors frequently report on borrowers receiving a ‘surprise’ notice of an unpaid real-estate tax bill or homeowner insurance bill, when they were under the impression that those payments had been included in their mortgage. Indeed, there are numerous reports of mortgage brokers and lenders employing the deceptive practice of marketing loans with an artificially low monthly payment by excluding the necessary tax and insurance costs; and then comparing the monthly payment to a ‘competing’ loan that does include taxes and insurance.

We do have some concerns about the provision to allow borrowers to opt out of the escrow after one year. We believe there is a risk that this could lead to deceptive practices in which a borrower is left with the impression that their mortgage payment is reduced after one year. If the opt-out provision is retained, we believe it is very important that the borrower be required to take affirmative steps to opt-out and that there be a full and transparent disclosure requirement to assure that the borrower fully understands their payment obligations in regard to the mortgages, as well as taxes and insurance. And, we are again concerned that this escrow requirement would be limited to subprime loans only. We believe this requirement should be extended to other nontraditional loans, such as “Payment Option Adjustable Rate Mortgages” and other Alt-A products.

### **Creditor Payments to Mortgage Brokers (Yield Spread Premiums)**

We applaud the Board’s proposal to prohibit yield spread premiums without written agreement between the broker and the borrower, but respectfully believe that this does not go far enough toward addressing a particularly troublesome practice in the mortgage industry.

NNA believes that the Federal Reserve should prohibit the use of yield-spread premiums. Since borrowers contract with and pay mortgage brokers, the borrowers are under the impression that the mortgage brokers are working for *them* – trying to find the most appropriate mortgage, at the best rate. The reality is that yield spread premiums create an absolute disincentive for mortgage brokers to identify the most appropriate and most affordable mortgage product for the borrower. Rather, yield spread premiums create an all too enticing incentive for mortgage brokers to steer borrowers to higher-rate loans than they qualify for, and all too frequently add prepayment penalties that lock them into those loans. The use of a yield spread premium places the economic interests of mortgage brokers in direct conflict with the interests of the borrowers. Only by eliminating the use of yield spread premiums would this inherent “conflict of interest” and the resulting distortions and unfairness in the mortgage markets be eliminated

NNA has also heard from mortgage brokers who claim that they are being unfairly singled out by the proposed provision that mortgage brokers should have to more fully disclose their compensation information to consumers. That issue would be eliminated if yield spread premiums were banned rather than disclosed. However, if the Federal Reserve decided to rely on disclosure alone, we believe it would be a mistake to exclude bank employees or any other loan originators (other than mortgage brokers) who offer mortgages from such disclosure.

### **Coercion of Appraisers**

NNA supports the Board's proposal in regard to prohibiting creditors and mortgage brokers from coercing appraisers to misrepresent the value of a consumer's residence. NNA is in full agreement with the statement in the Proposed Rule that says: *"A regulation under HOEPA that expressly prohibits creditors and brokers from pressuring appraisers to misstate or misrepresent the value of a consumer's dwelling would provide enforcement agencies in every state with a specific legal basis for action alleging appraiser coercion."*

### **Servicing Abuses**

NNA supports the Board's proposal in regard to servicing abuses.

### **Advertising Provisions**

NNA is supportive of each of the Board's proposals to amend the advertising rules.

One additional area we would encourage be tightened has to do with the deceptive advertising tactics associated with so called "no-cost" loans. An increasing number of lenders and brokers have been advertising mortgages with no points or additional costs. Borrowers are not told that they will end up paying a higher interest rate for the life of the mortgage, and end up paying much more than they would for other competing products. Over the term of a thirty year mortgage, the increased interest rate can amount to tens of thousands of dollars in additional charges to the consumer. While a so called "no-cost" mortgage may make sense for some borrowers, we believe lenders and/or brokers should have to provide more transparency in regard to the real costs associated with such mortgages. Perhaps simply permitting the use of a term such as "no-upfront-cost mortgage" (and banning the use of misleading terms such as "no-cost" mortgage) would help.

### **Mortgage Loan Disclosures**

NNA is supportive of the Board's proposal to extend the early mortgage loan disclosure requirement for residential mortgage transactions to other types of closed-end mortgage transactions, including mortgage refinancings, home equity loans, and reverse mortgages.

### **Closing**

I want to thank the Federal Reserve System for their efforts to protect consumers in the mortgage market from unfair, abusive or deceptive lending and servicing practices while preserving responsible lending and sustainable homeownership. This Proposed Rule has been introduced in the midst of one of the most challenging periods in the housing

markets since the Great Depression. I can appreciate the challenges faced by the Federal Reserve in attempting to stem abuses while not wanting to curtail responsible business practices through over-regulation. But at this point in our history, as the nation (and indeed the world-wide economy) continues to reel from the impact of the foreclosure crisis, I respectfully suggest that clear, decisive, consumer-oriented protections are called for. Now. More than ever.

Thank you for your consideration of these comments and for your efforts on behalf of consumers and the capital markets. Please feel free to contact me for any clarification of these comments.

Sincerely,



Eddie Latimer  
President



David C. Brown  
Executive Director