December 24, 2009

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

regs.comments@federalreserve.gov

Re: Proposed Amendments to Regulation Z, Rules for Closed-End Credit (Docket No. R-1366)

Dear Ms. Johnson:

The America's Mortgage Cooperative (AMC) appreciates the opportunity to comment on proposed amendments to Regulation Z issued for public comment by the Board of Governors of the Federal Reserve System (the Board). AMC is a member-managed cooperative that leverages the quality of 25 primarily regional mortgage lenders operating throughout the United States to improve their competitiveness in the marketplace to the ultimate benefit of their communities and customers. While the proposed rule constitutes a major revision of Regulation Z, AMC will concentrate its comments on the proposed changes to compensation practices for closed-end credit transactions.

AMC believes that the Board has identified legitimate issues with loan originator compensation and proposes a thoughtful solution. AMC shares the Board's objective of removing incentives for loan originators to "steer" borrowers to products and terms that are not in the borrower's best interest. Although the primary causes of abuses have removed by market forces (i.e. subprime and alt-A mortgage products), AMC recognizes that the Board is taking action to address long-standing concerns with originator compensation (overages/yield spread premiums) and to ensure that other harmful incentives do not develop again.

To accomplish this objective, the Board proposes prohibiting the mortgage lender ("creditor") or other third party from paying compensation to a loan originator (including a retail loan officer) "based on the credit transaction's terms or conditions". While the Board includes loan amount in this process, it is soliciting specific comments on this element of the rule.

With its proposal of a flat fee structure, the Board is effectively shifting the risk of loan originator overpayment from the consumer to the mortgage lender. While we recognize that mortgage lenders are better equipped than consumers to accept this risk, we hope the Board will consider the financial risk that this proposal places on mortgage lenders and will be as flexible as possible in implementing the final rule.

AMC's concern is based on the fact that loan officer and mortgage broker compensation has always been a variable cost meaning that total loan officer/broker compensation is tied almost entirely to loan revenue in the particular transaction. With the Board proposal, the mortgage lender will be required to pay loan originators the same compensation regardless of the loan revenue. Accordingly, while we understand the intent of the proposal is to remove any compensation incentives for loan originators charging prices above the lowest rate the lender is willing to accept, it does expose the lender to financial risk that previously did not exist (i.e. paying loan originators higher compensation than is justified from the financial data in the transaction).

AMC believes that there are significant differences in the level of harm created by the various loan conditions and terms. First, the most serious abuses occurred in the product area (subprime and alt-A pricing). As one study noted, over 50% of subprime borrowers could have qualified for prime (including government) mortgages. Moreover, in numerous 2006 speeches, OCC Comptroller John Dugan asked the simple question: Why would a consumer pay more not to submit income documentation (which should be readily available for most consumers)? The OCC also noted data indicated that more than 50% of subprime loans obtained stated income loans. While some consumers willfully participated in these schemes, loan officer compensation also played an important role in the proliferation of these high risk products.

As the Board notes in the preamble, "overages"/"yield spread premiums" occur when loans are originated at higher interest rates than is required by the lender/creditor. "Overages" (whether obtained by a retail loan officer or mortgage broker) have been a controversial issue for more than 20 years. "Overage" abuse (particularly on retail loans) has been reduced significantly because of the actions of federal regulatory policy.

As the Board demonstrates in its discussion of the loan amount issue (i.e. specifically soliciting comments), loan amount does not generate the same level of concern as the above two categories (particularly compensation by product type). AMC agrees with this view and believes few, if any, restrictions on loan amount are necessary for the following reasons:

1. The loan officer has minimal financial incentive to increase loan amounts.

   Even if the loan originator was so inclined, the opportunity for increased compensation is unlikely. For example, using the average existing house price is $172,600 (released this week by the National Association of Realtors) and a base compensation structure of 60 basis points, the maximum compensation difference between the widely available lowest downpayment program (3.5% for an FHA loan) and a 20% downpayment loan would be approximately $165. If the difference in loan amount was $5,000, the difference in compensation would be $30.

   We do not believe that a loan officer would even be motivated to jeopardize a transaction for an additional compensation of $30 to $165 (depending on the amount of increase in loan amount) when his/her total compensation would be approximately $800 to $1,000.

2. The Board's proposed restrictions on products will eliminate the incentive for a loan officer to steer the borrower to a product that has a more lucrative compensation structure.

3. There are countervailing forces at work that would deter any potential abuse.

   To obtain a higher loan-to-value ratio (above 80%), the consumer must pay for mortgage insurance. For example, to obtain a 3.5% downpayment using the FHA program, the borrower would be required to pay an upfront premium of 1.75% as well as annual premium of .55 percent. In addition to raising qualification concerns for the loan officer and the real estate agents, we doubt many borrowers would be willing to pay these costs unless they had no other choice.

   Consumers have tax incentives to maximize the loan amount. For many consumers, mortgage interest deduction is their primary tax benefit. Accordingly, it is often times in the borrower's interest to obtain an 80% LTV to maximize their tax benefit and reduce their tax liability.

   The new Home Valuation Code of Conduct (HVCC) has removed the loan originator from any role in the appraiser selection or payment process. The risk of inflated appraisals has diminished dramatically because of HVCC implementation.

In addition, permitting compensation based on loan amount would address a significant part of the concern raised earlier with regard to fixed costs. Since loan revenue is largely collected on a percentage basis, AMC believes it is fair and reasonable that expenses should be paid similarly.

Because the loan originator has no substantive incentive to promote higher balance loans, AMC also believes that mortgage lenders/creditors should be provided extensive flexibility with respect to loan amount. AMC believes:

1. Mortgage lenders should have the flexibility to pay different percentages of compensation for different loan amounts.
2. Mortgage lenders should have the flexibility to change the compensation schedule frequently (e.g. monthly) to minimize the downside risk associated the flat fee structure.
3. Mortgage lenders should be permitted to provide periodic bonuses (e.g. quarterly) based on volume and performance.

Finally, the Board grasps the concern of many mortgage lenders when it discusses the actions lenders take "to retain the consumer's business" on page 43283. While a lender could circumvent the intent of the rule by setting a high compensation level for a loan originator and then selectively lowering the compensation when necessary, AMC does not believe that flexibility for the lender to reduce loan officer compensation on a small percentage of loans (e.g. 10%) will undermine the intent of the rule. Moreover, the Board imposes recordkeeping on lenders that should facilitate monitoring of any abuses of an exception policy.

In conclusion, AMC appreciates the opportunity to comment on this proposed regulation. If you have any questions, please do not hesitate to contact our representative, Mr. Brian Chappelle. He can be reached at 202-637-7020.

Sincerely.

America's Mortgage Cooperative