Bank of America

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Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Attn.: Jennifer J. Johnson, Secretary
Docket No. R-1417
RIN No. 7100-AD75

Re: Proposed Rule Amending Regulation Z (Truth in Lending), Docket No. R-1417

Dear Madams and Sirs:

Bank of America appreciates the opportunity to submit this letter in response to the request of the Board of Governors of the Federal Reserve System (the "Board") for comments regarding its proposed rule amending Regulation Z, which implements the Truth in Lending Act (the "TILA"). Bank of America is one of the world's largest financial institutions and is actively engaged in facilitating the provision of credit to individual consumers, small- and middle-market businesses, and corporations.[1] In 2010, Bank of America extended $685 billion in total credit, including $298 billion in first residential mortgages and nearly $70 billion in residential mortgages to low and moderate income ("LMI") borrowers.[2] In 2010, nearly 1.4 million consumers obtained residential first lien mortgages from Bank of America. Similarly, in the first quarter of 2011, Bank of America extended $144 billion dollars in credit, including $57 billion in residential first lien mortgages to nearly 260,000 consumers and nearly $13.2 billion in LMI

[1] Bank of America originates residential mortgage loans through Bank of America Home Loans, Merrill Lynch Home Loans™, and U.S. Trust.
[2] Bank of America, Lending and Investing Initiative: Quarterly Impact Report (Fourth Quarter 2010), *available at* http://webmedia.bankofamerica.com/aheadbankofamerica/bank_of_america_q4_2010_qir.pdf.

residential mortgages.[3] In addition, Bank of America is actively involved in the securitization market, which provides the liquidity necessary to offer residential borrowers affordable mortgage loans. Since acting as the issuer of the first publicly registered offering of non-agency residential mortgage pass-through certificates in 1977, Bank of America has continued to act as a leader in the securitization market as an issuer itself and by providing underwriting, distribution, and advisory capabilities to clients.

In issuing the proposed amendments to Regulation Z (the "Proposed Rule"), the Board seeks comments on implementing those provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") that prohibit creditors from making loans without making a reasonable and good faith determination that the consumer will be able to repay the loan. The Proposed Rule also outlines the criteria for what constitutes a "Qualified Mortgage," which provides creditors with special protection from liability. It is generally believed that loans meeting the Qualified Mortgage standard will be substantially all of the mortgage market as creditors seek to minimize liability risk and provide affordable credit to borrowers.

We recognize and appreciate the importance of implementing a rule that provides effective protections to consumers while also fostering a robust and responsible residential mortgage market. Bank of America is fully invested in the return of a vibrant mortgage market that will help fuel the country's financial recovery. The ability of consumers to obtain affordable, reasonable mortgage products is, however, directly tied to the compliance costs and risks that creditors must incur in order to offer such loans. Concern that implementation of various regulatory proposals will limit a creditors' ability to sell loans in the secondary market has

[3] Bank of America, Lending and Investing Update (First Quarter 2011), *available at* http://webmedia. bankofamerica.com/aheadbankofamerica/v4/Reports/Bank%20of%20America%20Q1%202011%20LIU.pdf.

created market uncertainty. First and foremost, therefore, creditors are seeking clarity and certainty in the final rule because it will so significantly impact mortgage lending.

Given this need for certainty, it is critically important that the final rule provide a safe harbor for Qualified Mortgages and that the definition of what constitutes a Qualified Mortgage be clear, objective, and easily applicable. If the final requirements instead increase the liability exposure of creditors while at the same time providing only complicated methods of compliance, the result will be increased costs and further reduction in credit availability to the very consumers that the reforms were designed to protect.

In addition and without in any way minimizing the extensive efforts of the Board in developing the Proposed Rule, we believe that the Consumer Financial Protection Bureau (the "CFPB" or the "Bureau") should re-release a proposal for further comment once it has had the opportunity to review the present round of comments. As a result of the transfer of the Board's rulemaking to the CFPB on July 21, 2011, the Proposed Rule was drafted by one agency but will be finalized and implemented by another that was not even operational at the time the Proposed Rule was released. Given the paramount importance of the Proposed Rule's subject matter – the very ability of Americans to obtain residential mortgage credit – it is worth adopting a measured pace to ensure that the final rule is the best possible and that its full implications are explored to avoid unintended consequences. As a final rule is not required until eighteen months after the CFPB commences operations, there is ample time to undertake this analysis.

Finally, because the Proposed Rule's Qualified Mortgage definition is tied to the definition of Qualified Residential Mortgage ("QRM") contained in the Credit Risk Retention Proposed Rule, as discussed below, it is important that the CFPB have an opportunity to coordinate the definition of Qualified Mortgage with other federal agencies to ensure that its requirements are consistent with the QRM definition. To avoid any possibility of unintentionally conflicting standards, the CFPB should develop the Qualified Mortgage guidelines in conjunction with the QRM rule and should both reissue the proposed rule and adopt the final rule on the same timeline as the QRM rulemaking (which numerous comment letters have also requested to be reissued).

As a result, we ask the CFPB to build upon the excellent work of the Board while adding its own unique perspective to the rules and then allow interested parties to provide further feedback to assist the CFPB in fine-tuning the result. That approach ultimately will be more efficient than an iterative process of rapidly implementing a final rule and then responding to time-consuming requests for clarifications as the full implications of the rule become apparent.

I. The Proposed Rule Should Provide Clear and Objective Standards and a Safe Harbor for Qualified Mortgages

a. Certainty of compliance is critically important given the strong penalties imposed for violations

The Dodd-Frank Act adds new ability to repay requirements to TILA § 129C. The requirements seek to ensure that borrowers will have the financial resources to afford the loans they receive. As part of the new requirements, Dodd-Frank § 1416 applies the penalties originally created for violations of the Home Ownership and Equity Protection Act of 1994 (the "HOEPA") to violations of the new requirements for all closed-end mortgage loans. The HOEPA penalties allow consumers to recover an amount equal to all finance charges and fees paid, in addition to actual damages, statutory damages, and court costs and attorneys' fees. TILA § 130(a). Further, Dodd-Frank § 1413 creates new TILA § 130(k), which allows consumers to allege violations of the TILA § 129C ability to repay requirements as a defense in foreclosure actions involving the creditor or any assignee without regard to the statute of limitations. In combination with the expansion of the ability to repay requirements to cover all mortgage transactions, these penalties substantially increase the potential risks for creditors.

These substantial penalties make it critically important for creditors to have a clearly-defined, bright-line way of ensuring that the loans they make are in compliance with the new TILA provisions. Unless creditors can easily ascertain that the loans they offer to consumers comply with the Qualified Mortgage requirements, they will either be forced not to make the loans or to make the loans and pass the costs of uncertain legal risk on to consumers, raising the cost of borrowing and hindering economic recovery.

The importance of certainty is illustrated by creditors' historical experience with HOEPA and the Higher Priced Mortgage Loan guidelines (from which the TILA amendments and the Proposed Rule were derived). Largely because of the heavy legal risks for HOEPA violations and lack of a secondary market due to the potential for assignee liability, Bank of America does not intentionally originate HOEPA loans. Similarly, although TILA currently allows creditors to make so-called Higher Priced loans, the uncertain legal risks that attach to such loans generally limit their availability. The small number of loans is not, however, a function of the standards under which such loans can be originated, but rather is based on prudential concerns arising from the potential for significant penalties for violations of those standards.

The general ability to repay standards added by TILA § 129C and the Proposed Rule are likely to operate in a similar fashion. While Bank of America will originate some non-Qualified Mortgage loans under the general ability to repay rules, the numbers of such non-Qualified Mortgage loans will be relatively small and are likely to be retained on the balance sheet, as we believe no secondary market will exist for them. Generally, the only non-Qualified Mortgage loans originated will be to existing customers with demonstrated financial stability for whom creditors are able to make ability to repay calculations with a high degree of confidence. Outside of these individuals, the potential liability risks imposed by the Dodd-Frank Act likely will force creditors to originate only Qualified Mortgages. As with Higher Priced loans under the pre-Dodd-Frank Act regulatory regime, this limitation is not a function of how the Proposed Rules for ability to repay are drafted; rather, it is based on the high levels of compliance risk and possibility of penalties for violations in combination with the inherent long-term nature of mortgage loans.

b. The Qualified Mortgage guidelines must provide certainty through a safe harbor

Given the significant legal risks imposed for violations of TILA § 129C, the Qualified Mortgage provision must provide creditors with a true safe harbor to reduce compliance risks and to avoid raising costs to consumers unnecessarily. The supplemental information to the Proposed Rule asks whether the Qualified Mortgage provision should operate as a safe harbor or as a mere rebuttable presumption that loans meet the ability to repay standard. Bank of America strongly believes that a safe harbor Qualified Mortgage provision would strike the proper balance by providing borrowers with adequate protection while still allowing creditors to satisfy their compliance obligations with a sufficient degree of certainty. As the Board correctly acknowledges, "the drawback" of a mere rebuttable presumption Qualified Mortgage rule "is that it provides little legal certainty for the creditor, and thus, little incentive to make a 'qualified mortgage.'"[4] Without such bright-line objective standards, the expansion of HOEPA penalties to the entire residential mortgage market as mandated by Dodd-Frank § 1416 will reduce the availability of consumer credit and unnecessarily increase the costs of borrowing for consumers. The primary purpose of the Qualified Mortgage rule is to recognize that certain types of loans are

[4] 76 Fed. Reg. 27,396.

safe for consumers and thus do not require the same degree of regulation as less traditional loans. Given that purpose, there is no need to increase uncertainty – and thus costs to consumers – for Qualified Mortgages.

To meet these important goals of providing certainty and proper incentives to make Qualified Mortgages, we strongly support the provisions of the Proposed Rule's Qualified Mortgage Alternative 1, 12 C.F.R. § 226.43(e), subject to the clarifications suggested below. By providing for a safe harbor, Alternative 1 meets the critical need for certainty in lending as well as proper incentives for originating "traditional" residential mortgage loans where possible. Creditors can easily identify whether a loan has negative amortization, interest-only payments, or balloon payments because those terms are readily identifiable on the face of the loan documents. Similarly, the term of a loan is readily apparent, and creditors can easily ensure that they are making loans with terms not exceeding thirty years. Other proposed criteria, however, are not as objective and have the potential to undermine the security of the safe harbor. The points and fees test (as further addressed below) has the potential to minimize the value of a safe harbor for lenders. We believe that if such a test is required as part of the final rule, it must be tied directly to information that is disclosed as part of the transaction and is easily calculable for the creditor, the borrower, and any subsequent purchaser of the mortgage loan. Therefore, tying the calculation to specific fields of the HUD-1 closing statement required by the Real Estate Settlement Procedures Act (the "RESPA"), for example, provides a degree of certainty for all parties. Including fees that are not easily identifiable (for example, retail loan originator compensation or fees incurred after loan closing), on the other hand, has the potential to create enormous uncertainty and therefore fails to set an objective standard.

c. Certainty is also critical for secondary mortgage market financing

i. The secondary mortgage market makes low-cost borrowing possible for consumers through securitization

Certainty is also a necessary prerequisite to assure liquidity for creditors and to enable a secondary market for residential mortgage loans to operate. Traditionally, most residential mortgages are securitized, either through Government Sponsored Entities ("GSEs") like Fannie Mae and Freddie Mac or through private market securitization. Such securitization provides necessary market liquidity that allows mortgage creditors to obtain capital to make loans to consumers. That liquidity, in turn, benefits consumers by allowing residential mortgage creditors to provide the lowest possible cost of borrowing.

Certainty is particularly important to investors who purchase securitized residential mortgage loans. Investors will be understandably reluctant to purchase securities backed by loans that may be subject to foreclosure defenses and enhanced damages (due to assignee liability) based on criteria that cannot be readily and accurately determined by stakeholders involved in a secondary market purchase. As a result, it is important that the Qualified Mortgage definition provide a clear, objective safe harbor that will allow investors in securitized residential mortgage loans to verify that they are not purchasing compliance risk along with their investments.

As part of securitization, investors and rating agencies alike must be able to evaluate the risks embodied in a security. If there is uncertainty about such a fundamental issue as to whether the mortgage loans underlying a securitization are Qualified Mortgages or not, and thus whether they are subject to the foreclosure defense for failure to meet the ability to repay standard, it will be increasingly difficult to sell or securitize these loans. Rating agencies will have difficulty evaluating the unquantifiable risk related to the availability of such a defense for the life of the loan, investors will be uncertain what lurking compliance risk they are purchasing, and ultimately borrowers may be unable to obtain funding as a result. In turn, that inability to obtain funding will flow back to borrowers as increased borrowing costs. If the Proposed Rule does not operate as an objective safe harbor, the resulting uncertainty will eliminate the efficiencies provided by secondary sale or securitization of these loans and, by extension, to the cost of borrowing for consumers.

ii. The Qualified Mortgage definition should be as broad as possible because it will impact securitizers' Qualified Residential Mortgage risk retention obligations under Dodd-Frank § 941

It is also critically important to foster a viable secondary mortgage market by recognizing that the Qualified Mortgage definition impacts the definition of Qualified Residential Mortgages ("QRM") embodied in the Risk Retention regulations required by Dodd-Frank § 941. As relevant here, the Risk Retention regulations require all residential mortgage securitizers to retain risk on securitizations, but they also contain an exception for securitizations containing QRMs, intended to be the safest and most creditworthy loans in the marketplace. There are a number of requirements for a loan to qualify as a QRM, but an important requirement in Dodd-Frank § 941 is that the QRM definition can be "no broader than the definition of 'qualified mortgage' as the term is defined under § 129C(c)(2) of the Truth in Lending Act." § 941(e)(4)(C). It could be argued that the effect of this requirement is to incorporate the definition of the Qualified Mortgage rule, including its 3% limitation on points and fees, into the QRM definition. Because the QRM definition proposed pursuant to Dodd-Frank § 941 is already narrow, any further narrowing as a result of the Qualified Mortgage regulations adopted here could result in substantial negative consequences for the housing industry and consumers.

d. Product type is not representative of the ability to repay, and the Qualified Mortgage rule should not exclude specific loan products

As we have previously noted, mortgages that meet the Qualified Mortgage standard will be the predominant mortgages available in the market. A Bureau representative recently stated that it is not the intention of the Bureau to ban any particular product type outright. The Qualified Mortgage definition, however, specifically excludes certain mortgage loan products. The result is that such products will not be available in the general mortgage market. Consistent with the intent of the rule, creditors' general experience shows that loans appropriately documented and underwritten in accordance with established policy are effective predictors of the borrowers' ability to repay. Generally this is true without regard to product type. The fixed rate, interest only loan, for example, while only a small portion of overall production, is a useful product for many consumers. The product offers lower monthly payments, tax advantages, and a reset with a long window before refinance (e.g., after ten years), providing a great deal of flexibility to consumers. With appropriate documentation and underwriting restrictions (underwriting to a fully amortizing payment, for example), these loans continue to perform well and should not be eliminated from the market by being designated as non-Qualified Mortgages. Further, TILA and Interagency Guidance already mandates underwriting to reduce "payment shock" and to otherwise ensure that customers can make their mortgage payments well after the loan closes. Therefore, ample consumer protections are already in place for non-Qualified Mortgages.

Similarly, while not specifically excluded by the definition, adjustable rate mortgages with start rate periods shorter than five years will also be effectively eliminated from the market. The Proposed Rule has set a more stringent test for borrowers to qualify for an adjustable rate mortgage and still qualify under the Qualified Mortgage test. The direct impact will be that the availability of products with initial periods less than five years will be significantly reduced. We encourage the Bureau to revisit the Qualified Mortgage standard and to implement a requirement that the borrower qualify by using the higher of the start rate plus 2% or the fully indexed rate at loan closing.

e. The Alternative 1 safe harbor should consider consumers' repayment performance over time

Further, we encourage the Bureau to give creditors the full strength of a safe harbor by including criteria which look at consumers' repayment performance on mortgage loans over time. Many creditors are concerned that for every foreclosure action initiated after the implementation of this rule, creditors will need to defend against the allegation that the Qualified Mortgage safe harbor does not apply or that there has been a violation of the general ability to repay standards. We believe that such allegations often will relate to a technical compliance error that has no bearing on whether the consumer actually had the ability to repay the loan at the time of origination. The Proposed Rule is intended to guarantee that borrowers have the ability to repay the loans that creditors underwrite, and a borrower who has made payments for an extended time period has clearly demonstrated that he possessed the ability to repay at the time that the loan was made. Defaults that occur after a borrower has already made years of mortgage payments presumably are not the result of underwriting decisions. Instead, such defaults are likely caused by uncontrollable macroeconomic or life event incidents, such as housing market trends, natural disasters, illness, death, divorce, factory closings, or the health of the employment market generally. Creditors should not be held responsible for subsequent events over which they have no control.

To reflect these facts, the Qualified Mortgage safe harbor rule should contain a provision addressing borrowers' demonstrated ability to repay the loan. If the borrower has made timely payments (including payments within the mortgage loan grace period) for 24 months, the safe harbor should be valid even if it is subsequently determined that the creditor made a compliance error. For example, if the loan inadvertently violated the 3% points and fees test or the creditor relied on a borrower's documentation rather than verifying with a third party, the creditor nevertheless should have the benefit of the safe harbor if the borrower has demonstrated that the creditor's underwriting decision was sound by making timely payments for some extended period of time.[5]

II. Calculation of the 3% Points And Fees Limitation

We are also concerned about the 3% limitation on points and fees in the Qualified Mortgage rule. As an initial matter, points and fees simply are not a good predictor of ability to repay and should not be included in the Qualified Mortgage requirements. Those requirements are intended to ensure that residential mortgage loans are well-underwritten and that borrowers can afford to make their mortgage payments. Points and fees are one-time charges that in no way reflect borrowers' ongoing financial health. Additionally, the protections provided in the Qualified Mortgage definition that limit product type and require income verification are more than sufficient to ensure repayment ability. As a result, we request the Bureau to use the extensive general rulemaking authority Congress granted for purposes of developing the Qualified Mortgage rule to modify this requirement. See TILA § 129C(b)(3)(B)(i). The Board has properly exercised this authority in various instances in the Proposed Rule. The authority grants the power to "prescribe regulations that revise, add to, or subtract from the criteria that define a qualified mortgage upon a finding that such regulations are necessary or proper to ensure that responsible, affordable mortgage credit remains available to consumers" throughout

[5] See the General Accounting Office's report "Potential Impacts of Provisions in the Dodd-Frank Act on Homebuyers and the Mortgage Market," GAO-11-56, at 59 ("With respect to rulemaking efforts, NCUA expressed concern about the lack of a mechanism for non-QMs to receive QM status after some period of performance given the potential difficulty some borrowers, including those of modest means, may have in meeting the QM criteria. NCUA suggested that creating such a mechanism could help achieve the goal of protecting borrowers from unsustainable mortgage products while maintaining broad access to mortgage credit.").

the drafting of the Proposed Rule. *Id.* We believe the authority to be equally applicable to the Bureau in completing the task begun by the Board.

However, if the Bureau decides to include a points and fees limitation on Qualified Mortgages, there are a number of considerations that must be met to avoid substantially reducing the availability of credit to borrowers. Because Qualified Mortgages are likely to be substantially all of the mortgage market, it is critically important that the points and fees requirement, if included in the Qualified Mortgage definition, be defined to avoid cutting off access to credit for large numbers of consumers.

We believe that the current and widely accepted GSE calculations of points and fees for mortgages originated and delivered under the GSE guidelines are consistent with the protections that should be provided for consumers. As a result, we recommend that the Board eliminate the points and fees test in the Proposed Rule entirely in favor of a Qualified Mortgage definition based on the tested and workable standards currently imposed by the GSEs. Notwithstanding this recommendation, at a minimum as discussed below, we believe that Loan Level Price Adjustments and loan officer compensation should not be included in the Qualified Mortgage points and fees calculation. Additionally, because points and fees are calculated as a percentage of loan balance, we believe that adjustments to the Qualified Mortgage rule's proposed definition for small principal balance loans are necessary to permit all homeowners access to these loans.

a. The current Proposed Rule properly calculates total loan amount for purposes of the points and fees test; the points and fees test should be limited to charges collected at or before loan closing

Under the Proposed Rule, "total loan amount" is calculated by taking the "amount financed" (as determined under Regulation Z) and deducting certain costs listed in 12 C.F.R. §§ 226.32(b)(1)(iii) and (iv) to the extent that these costs are both included as points and fees and financed by the creditor. The Board requested comment on whether to streamline the calculation to better ensure that the "total loan amount" includes all credit extended other than financed points and fees. Specifically, the Board solicited comment on whether to revise the calculation of "total loan amount" to be the following: "principal loan amount" (as defined in 12 C.F.R. § 226.18(b)), minus charges that are points and fees under 12 C.F.R. § 226.32(b)(1) and are financed by the creditor. We believe that the calculation of the "total loan amount" set forth in the Proposed Rule should remain unchanged rather than adopting the alternative offered by the Board. While understanding the Board's rationale for the alternative approach, we believe that the proposed alternative would have a detrimental impact on mortgage loan refinancing, where borrowers often finance their points and fees. In particular, this change would have the most acute impact on borrowers with smaller loan balances and their ability to obtain a Qualified Mortgage.

The Board also requested comment on whether fees should be included only if payable at or before closing as the Dodd-Frank amendments do not contain such a limitation. The Board expressed concern that without such limiting language, the points and fees calculation could be deemed to include some post-closing fees, such as fees to modify a loan. Introducing such uncertainty into the calculation of a points and fees test would create huge uncertainty and would severely diminish the value of a safe harbor under the Qualified Mortgage test. We encourage the Bureau to ensure that the only fees that can be included in the calculation are those known at closing.

b. Loan level price adjustments ("LLPAs") should be excluded from the Qualified Mortgage points and fees calculation

The Board requested comment regarding whether loan level price adjustments ("LLPAs") should be included in the Qualified Mortgage points and fees calculation. We strongly believe that they should not be included. LLPAs are risk based pricing adjustments that are used by creditors to compensate for borrower or loan characteristics that create layered risk. For instance, an LLPA might be layered into the mortgage rate that a borrower is offered if the borrower's loan size exceeded a certain amount. LLPAs are intended to reflect the potentially greater risk associated with a given mortgage loan. In the present market, non-GSE LLPAs typically are made by adjustments to the rate that a borrower pays, rather than as points. As a result, they are not points or fees and should not be included in the 3% calculation for Qualified Mortgages. In addition, because such adjustments are not obvious from the face of the loan documents, including them in the points and fees calculation for Qualified Mortgages could create a substantial litigation issue that could only be resolved through extensive discovery and trial, creating dramatic uncertainty. For these reasons, LLPAs should not be included in the Qualified Mortgage points and fees calculation.

As noted earlier, we believe it is very important that the Bureau have the opportunity to coordinate with the agencies responsible for the Credit Risk Retention Proposed Rule in order to avoid unintended regulatory difficulties. This is especially true with regard to the interaction between LLPAs and the complex requirements of the Premium Capture Cash Reserve Account (the "PCCRA") currently embodied in the Credit Risk Retention Proposed Rule.[6] As explained in Bank of America's July 13, 2011 Comment Letter on the Credit Risk Retention Proposed Rule, the PCCRA as currently drafted effectively prevents creditors from securitizing any mortgage with a rate that would result in premium securitization prices. The PCCRA rule would require any premium in the price of a securitization backed by residential mortgage loans, regardless of whether it was the result of general market movements, proceeds to the creditor, or even reimbursement for the creditor's basis in the loan, to be placed in a first loss position in the

[6] For an extensive discussion of the Credit Risk Retention PCCRA and its impact on the residential mortgage market, see Bank of America's Comment Letter on the Credit Risk Retention Proposed Rule (July 13, 2011), at 13-33 & Appx. B, *available at* http://fdic.gov/regulations/laws/federal/2011/11c84ad74.PDF.

securitization. The effect is to make premium loans too expensive to originate. As a result, we do not expect creditors to be able to make LLPAs through rate adjustments if the PCCRA rule is included in the final Credit Risk Retention rule.

If this occurs, LLPAs would have to be made through points and fees adjustments. However, if LLPAs are included in the points and fees calculation of the Qualified Mortgage definition, the proposed rule effectively will pin creditors into a corner. The PCCRA Risk Retention rule will prevent paying for LLPAs through rate. Using points and fees to compensate for LLPAs instead, in conjunction with the points and fees already included in the Qualified Mortgage calculation, would push many loans over the 3% threshold. In short, if LLPAs are included in the Qualified Mortgage points and fees calculation, the Qualified Mortgage rule, coupled with the effects of the PCCRA, will have the direct cause of reducing credit availability to a substantial number of consumers. To avoid this dramatic result, LLPAs should be specifically excluded from the Qualified Mortgage points and fees calculation.

c. Loan officer compensation should not be included in the 3% points and fees limitation

Proposed Rule § 226.32(b)(1)(ii) proposes to include loan officer compensation in the calculation of points and fees for Qualified Mortgages. We do not believe this requirement is appropriate. Its only effect will be to create difficulties in the calculation of points and fees at the time of loan origination and ultimately to reduce the number of borrowers who are able to qualify for affordable Qualified Mortgages.

As an initial matter, creditors already consider loan officer compensation as an overhead variable when determining how to price a loan overall. After all, employee compensation is always a cost of business and must be covered by revenue if a business is to remain viable. As a result, loan officer compensation is already included in the cost of the loan. If included as a separate variable, any loan officer compensation essentially will be double counted.

Similarly, it is not necessary to regulate loan officer compensation through the Qualified Mortgage rule because perceived abuses have already been addressed by the recent implementation of the Board's loan originator compensation rules (12 C.F.R. § 226.36). Title XIV of the Dodd-Frank Act includes similar restrictions against allowing loan originator compensation based on transaction terms or conditions. As a result of the Board's rule, creditors have removed any tie between products, pricing and originator compensation. Inclusion of loan officer compensation in points and fees calculations, therefore, is redundant from a consumer protection perspective.

The blanket inclusion of all loan officer compensation, whenever paid, will also make it impossible to calculate points and fees at the time of loan origination. Although Proposed Comment Paragraph 32(b)(1)(ii)[7] states that loan officer compensation is only included in the Proposed Rule's 3% calculation if it can be determined at or before loan closing, the examples given as representative in that paragraph will not always be capable of being calculated until long after closing. The paragraph's Example C illustrates the problem. Because many bonuses are based on the total production of a loan officer for the bonus period, in many instances full loan officer compensation will not be known until bonuses are paid at the end of the month, quarter, or year (depending on bonus schedules). As a result, prudent creditors will be forced to limit points and fees well below the 3% threshold to allow for the possibility that loan officers will receive their maximum possible compensation, regardless of whether it is actually earned and paid at a later date. That result will limit the availability of Qualified Mortgage credit to borrowers unnecessarily. Similarly, even in situations involving the same creditor and same loan

[7] 76 Fed. Reg. 27,488.

officer, identical loans will be subject to different points and fees calculations if the loan officer receives tiered bonuses for heightened productivity. For instance, Example C states that the compensation of a loan officer who receives no bonus for his first ten transactions is not included in points and fees, but if the eleventh loan entitles the officer to a bonus, that bonus must be included.[8] This rule would apparently apply even if the tenth and eleventh loans were otherwise identical.

As discussed above, including loan originator compensation creates uncertainty in what should be objective rules. We strongly encourage the adoption of a final rule that looks squarely at the documents included in the loan closing to determine whether the loan meets the Qualified Mortgage test. For the points and fees test, this would include the appropriate fees required for the calculation that are disclosed on the HUD-1 settlement statement provided in connection with the transaction.

Finally, it will be highly problematic and burdensome to add tracking of loan officer compensation at the transactional level (as proposed). That requirement would force creditors to add systems to tie information about the compensation of each of their loan officer employees to the loan files of every loan made. The complexity would increase even more in the event that a creditor acquired a loan made by another organization. Especially in light of the other significant problems with including loan officer compensation in points and fees that are addressed below, these additional burdens are simply unwarranted.

In short, there is no reason to include loan officer compensation in the 3% points and fees calculation for Qualified Mortgages. That limitation will not provide any additional protections for consumers but will create uncertainty in application of the rule and will instead lower the number of loans that can be made to consumers.

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[8] *Id.*

d. Bona fide settlement service fees are necessary for originating loans and should not be included in the 3% points and fees limitation, regardless of whether they are paid to affiliates or non-affiliates

We wholeheartedly agree with the Proposed Rule that bona fide charges incurred for the services of non-affiliated third parties in originating loans should not be included in the 3% points and fees calculations for Qualified Mortgages, as provided in Proposed Rule § 226.43(e)(3)(ii)(A). Charges for services such as appraisals, credit reports and title insurance are necessary to issuing loans and have no impact on borrowers' ability to repay. In addition, in many cases such fees are already controlled by federal and state regulation (including new limitations on appraisal fees adopted by the Dodd-Frank Act). As such, they should not be included in the points and fees calculation.

Therefore, and for the same reasons, we believe that similar fees paid to a creditor's affiliate should likewise be excluded. The Qualified Mortgage points and fees test should allow for equal treatment of settlement service providers, without regard to their ownership structure. The Proposed Rule's disparate treatment would reduce the ability of creditors to control the quality of ancillary settlement services and would negatively impact both consumers and the economy.

A large number of the nation's leading national lenders, real estate brokerage firms, and homebuilders offer both mortgage loans and other settlement services through wholly owned subsidiaries, affiliates, or joint ventures. These entities must comply with the affiliated business arrangement provisions of RESPA. The negative impact of this requirement will be most keenly felt by those borrowers seeking smaller loan balances as it will be very difficult for creditors relying upon affiliates for settlement services to originate such loans cost effectively.

For many years, RESPA has been based on a policy that permits creditors to require the use of a settlement service provider for core services (i.e., appraisal, credit reporting, and attorney services) used in the origination of mortgage loans. To the extent that creditors can use their affiliates for these and other settlement services, they have significantly greater control over the quality and compliance standards under which loans are produced. This quality control benefits both creditors and their mortgage customers and investors. The proposed Qualified Mortgage points and fees test will effectively overturn RESPA's well-established policy and weaken the ability to closely monitor the quality, efficiency, consistency, and legal and regulatory compliance of settlement services, as required under the Office of the Comptroller of the Currency's long-standing guidance regarding the management of third parties. For these reasons, charges for settlement services provided by an affiliate should also not be included in the calculation of points and fees.

We recognize that the language of TILA § 129C(b)(2)(C)(i) only exempts third-party charges for non-affiliates of creditors or originators. However, we believe that the Bureau should use the extensive discretion that Congress granted to it in TILA § 129C(b)(3)(B)(i), discussed above, to modify this requirement. Pursuant to that broad authority and with an aim to avoid unnecessarily raising costs to consumers and to maintain creditor flexibility, bona fide fees paid to affiliates of mortgage creditors for services rendered should be exempted from the 3% points and fees calculations.

e. The points and fees limitations for mortgage loans with principal balances below $150,000 should be 4% to avoid unnecessarily penalizing individuals with small loans

Because the Qualified Mortgage points and fees calculation is based on a percentage of loan principal balance, while mortgage origination costs tend to be relatively constant regardless of loan size, borrowers with small loan balances will be unduly impacted unless an alternative calculation is provided. We agree with the Board's decision to provide such an alternative

Qualified Mortgage calculation in Proposed Rule § 226.43(e)(3)(i). However, we suggest several changes in order to make the exception more meaningful to likely borrowers.

The Proposed Rule sets the cut-off for a low principal balance loan at $75,000. We believe that cut-off is too low and should be raised to $150,000. If a loan with a principal balance of $75,000 is subject to the standard 3% points and fees limitation, many borrowers will be priced out of low-cost Qualified Mortgages. Presumably, borrowers with smaller principal balances will also tend to be lower income borrowers, and the ability to place such borrowers into the lowest possible cost Qualified Mortgage loans will be critically important.

The Proposed Rule also suggests two alternative methods of calculating permissible Qualified Mortgage points and fees for small balance loans. Respectfully, we believe that both methods are unnecessarily complex and would be prohibitively difficult to scale in order to provide loans to meaningful numbers of consumers. Instead, we believe that a flat 4% points and fees limitation should be adopted for Qualified Mortgages with principal balances below $150,000. Such a limitation is straightforward and easy to apply, and its simplicity will ultimately enable creditors to provide financing to smaller balance loans with more certainty of their Qualified Mortgage status, ultimately benefitting consumers by allowing the lowest possible borrowing costs.

f. Borrower paid mortgage insurance and voluntary borrower paid insurance products should be excluded from the Qualified Mortgage points and fees calculation

We agree in principal with the Proposed Rule that up front mortgage insurance premiums should be excluded from the points and fees calculation. However, we believe that the entire premium for borrower paid private mortgage insurance should be excluded, not merely the comparable amount payable under policies in effect at the time for FHA loans. See Proposed Rule § 226.32(b)(1)(i)(B)(2). Furthermore, we do not believe that exclusion should be conditioned upon the premium being refundable on a pro rata basis and automatically issued upon notification of the satisfaction of the mortgage. These conditions will undercut the ability of creditors to exclude up front mortgage insurance premiums from the points and fees limitations.

Borrower paid mortgage insurance is an alternative for borrowers who cannot afford a significant down payment. Consider two hypothetical borrowers taking out identical loans. One borrower has the cash to pay for a full 20% down payment, while the other borrower can only afford 10%. If the second borrower is required to have mortgage insurance as a result of the lower down payment while the first borrower is not, the mortgage insurance effectively serves as a down payment substitute and should not be included in the points and fees calculation. To do so would penalize the second borrower simply because he has less available cash. In addition, to the extent that any portion of borrower paid up front mortgage insurance is included in the points and fees calculation, it is likely to disproportionately impact LMI borrowers and others who are least able to afford the price increases associated with non-Qualified Mortgage borrowing.

The Board also solicited comment on whether guaranty fees for federal loan programs should be excluded from the points and fees calculation. We agree with the Board's proposal to exclude guaranty fees from the calculation as we believe that inclusion of such fees would mean that such loans (e.g., VA and FHA) would have a much higher propensity to exceed the points and fees threshold.

The Board solicited comment on the proposal to implement the statutory provision that includes up front premiums and charges for credit insurance and debt cancellation and suspension coverage. We believe the Bureau should exclude such premiums or charges from the points and fees test when such premiums or charges are for optional coverage. On the other hand, if a creditor requires any such coverage, premiums or charges paid at or before closing should be included in the points and fees test.

g. Lending to borrowers with demonstrated financial stability

As the Board noted, the purpose of TILA § 129C is to "assure that consumers are offered and receive residential mortgage loans on terms that reasonably reflect their ability to repay the loans." Dodd-Frank Act § 1402. Portfolio lenders often work with consumers with demonstrated financial stability as evidenced through their longstanding banking, fiduciary, or brokerage relationships. These consumers typically have a very strong repayment history, reflecting their substantial assets and resultant strong ability to repay. Creditors with such relationships have a clear picture of borrowers' overall financial situations based on the ongoing review and analysis undertaken as part of account management.

The Board proposed commentary provisions that would allow creditors to evaluate consumers' repayment ability by looking to widely accepted governmental or nongovernmental underwriting standards. We believe it is important for any final rule to specifically retain the capacity for creditors to comply with Regulation Z's "ability to repay" requirement by documenting and underwriting loans in accordance with generally observed underwriting standards. Widely accepted underwriting standards ensure that creditors may rely upon information of which they have knowledge, as well as information that can reasonably be obtained by a review of the consumer's credit application or through information obtained by the creditor utilizing generally accepted standards for due diligence review. It specifically includes information that can be obtained from, or based upon, the creditor's management of the consumer's financial accounts. This is especially true for consumers requiring customized loans underwritten to correspond to their personal financial profile and needs. Such loans are highly creditworthy but not conventional as such a concept is currently embraced under the Qualified Mortgage rule.

Alternatively, we encourage the Bureau to consider modifying the Qualified Mortgage safe harbor to include loans made to, or guaranteed by, consumers with Demonstrated Financial Stability ("DFS"). While there are a number of ways the final rule could define DFS consumers, one potential definition might incorporate the Securities and Exchange's (the "SEC") standard set forth in Rule 501 for Accredited Investors.

Creditors generally maintain loans made to DFS consumers in their portfolio which further aligns the interest of the DFS consumer and the creditor in ensuring the consumer has the ability to repay. Without Qualified Mortgage treatment, however, creditors will be required to take on additional legal risk to make these custom mortgage loans which will affect both cost and availability of such customized loan structures. Lack of Qualified Mortgage treatment may also impact the safety and soundness of portfolio creditors to the extent the potential legal risk of such loans makes them unsalable.

As we noted earlier, we encourage the Bureau to not specifically exclude product types from the Qualified Mortgage standard. This is particularly relevant with DFS consumers who are more likely to utilize products like interest only mortgages and balloon loans to meet their financial needs.

III. Ability To Repay Comments

a. The Proposed Rule properly allows income to be verified by third-party documentation provided by borrowers

We agree that income verification is an important part of Alternative 1, and we therefore agree that creditors should be able to verify income for purposes of the ability to repay rule by receiving and reviewing the documentation listed in Proposed Rule § 226.43(c)(4)(i)-(vii), including a copy of a borrower's IRS Form W2, tax returns, or payroll receipts.[9] In addition, we strongly agree with the commentary in Paragraph 43(c)(3) stating that "[c]reditors also may obtain third-party records directly from the consumer. For example, creditors using payroll statements to verify the consumer's income (as allowed under Proposed Rule § 226.43(c)(4)(iii)) may obtain the payroll statements from the consumer."[10] We believe that creditors should have the ability to rely on third-party income documentation provided by borrowers. While we agree with the Proposed Rule that income verification obtained directly from third parties should also be allowed, it should not be required. Creditors should be able to rely on borrowers' representations that the official documents they provide accurately reflect their income, and the Proposed Rule should expressly permit such reliance.

b. Community seconds (and similar products) should not be included in the ability to repay requirements

As a general rule, creditors must make a reasonable and good faith determination that, at closing, the borrower has a reasonable ability to repay the loan, including any existing or new subordinate liens and all taxes, insurance and assessments. While recognizing the need to consider new or existing subordinate liens, there are certain types of second lien obligations that merit an exclusion from the ability to repay calculation. These loans are second mortgages intended to promote home ownership in underserved communities and include "community seconds," down payment assistance programs, and employer home ownership assistance loans.

These loans typically are used to assist borrowers who could not otherwise afford home ownership by providing funds for a down payment. As a result, these loans often include forgivable features, do not require regular principal and interest payments, or are due solely upon

[9] Proposed § 226.43(c)(4) relates to income calculation for the general ability to repay rule, but proposed § 226.43(c)(2)(v) cross-references § 226.43(c)(4) and indicates that the same income calculations also apply to Alternative 1 of the Qualified Mortgage standards.
[10] 76 Fed. Reg. 27,494.

sale of the home. Community groups, nonprofits, employers, and others have determined that these loans promote goals that are not entirely economic and assume the risk necessary to attain those non-economic ends. As these loans are different than the typical second mortgage loan, they should not be included in the borrower's debt obligations when performing the ability to repay calculation. If the ability to repay calculation includes these types of loans, it will negatively impact the prospect of home ownership in many low- to moderate-income communities and frustrate the intent of those endeavoring to support such communities. To avoid this negative impact, we recommend that the final rule exclude from the ability to repay criteria, any debt obligations associated with a second mortgage loan extended by a nonprofit organization, state housing finance, community group, or employer for the purpose of assisting a borrower with the purchase of a principal residence from consideration under the ability to repay determination.

c. Flexibility in inclusion of current debt obligations and consideration of repayment history in the general ability to repay standards

While we generally believe the great majority of lending will be made under the Qualified Mortgage standard, we still encourage the Bureau to provide a reasonable amount of latitude in the underwriting process under the general ability to repay standards. For example, the Proposed Rule requires inclusion of all student loans. Most lenders offer loan programs which exclude student loans from the calculation of current obligations if payment for the student loan is deferred for more than 12 months. We also note that the current government sponsored Home Affordable Refinance program allows borrowers to be qualified if they demonstrate successful payment of their existing mortgage as ability to pay, rather than looking solely to debt to income ratios or residual income. We encourage the Bureau to give full consideration to guidelines that allow creditors to consider successful payment on the same or a higher existing mortgage payment or housing obligation.

IV. Refinancing of Non-Standard Mortgages

The Dodd-Frank Act provides an exception to the ability to repay standard's underwriting requirements if: (1) the same creditor is refinancing a "hybrid mortgage" into a "standard mortgage," (2) the consumer's monthly payment is reduced through the refinancing, and (3) the consumer has not been delinquent on any payment on the existing hybrid mortgage. The Proposed Rule implements this exception with the following conditions:

a) The creditor must be the current holder or servicer of the non-standard loan;

b) The new monthly payment must be "materially lower" than the current monthly payment;

c) The creditor must receive the written application before the fixed rate period ends on an adjustable rate mortgage loan;

d) The consumer must not have made more than one 30 day late payment on the non-standard loan during the twenty-four months immediately preceding the creditor's receipt of the written application; and

e) The consumer must not have made any 30 day late payments in the six months immediately preceding the creditor's receipt of the written application.

We strongly agree that an exception to the ability to repay standard's underwriting requirements should exist for streamlined refinancings. This exception will help borrowers stay in their homes by encouraging creditors to make streamlined refinancings to troubled borrowers. Because streamlined refinancings have substantially increased in recent years, we believe that additional flexibility is necessary to accommodate borrowers at risk of default and foreclosure.

To provide this additional flexibility, we recommend several changes to the exception in the Proposed Rule. First, the subservicer of the loan should be eligible to be the creditor with respect to the standard loan in addition to the current holder or the servicer. Second, refinancing should be permitted after the loan is recast. This flexibility will benefit borrowers who were unable to refinance before the recast but are only able to make the new payments for a short period of time. Third, allowing only one 30 day late payment in the past 24 months on the existing mortgage is too restrictive and would require the creditor to overlook timely recent payments. We believe that a 12-month period would be more appropriate and indicative of the borrower's commitment and ability to pay. Fourth, the current prohibition on any late payments in the past six months should provide some flexibility in the event of extenuating circumstances. Fifth, refinancings extended under any HUD- or GSE-sponsored streamline financing program should be eligible for this ability-to-pay exception. Finally, while the Dodd-Frank Act expressly contemplated the refinancing of hybrid mortgages into standard mortgages, the ability to refinance an existing standard mortgage into a new standard mortgage (meeting all of the conditions established by the final regulation) would help some borrowers remain in their homes. Therefore, we would recommend that the Bureau use its discretion to permit such refinancings for standard mortgage loans.

V. Conclusion

We are grateful for the chance to provide these comments to the Proposed Rule. If there are any questions arising from our comments or any other aspect of this topic, we welcome the opportunity to provide assistance in any way that is helpful. Please feel free to contact Mary Jane M. Seebach (mary.jane.seebach@bankofamerica.com, 818-223-5662) or the undersigned (kenneth.l.miller@bankofamerica.com, 980-386-6669) at any time.

Respectfully submitted,

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