Consumer Mortgage Coalition

December 23, 2010

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 Proposed Rule – Open-End and Closed-End Loans
Docket No. R-1390

Dear Ms. Johnson:

The Consumer Mortgage Coalition (CMC), a trade association of national mortgage lenders, servicers, and service providers, appreciates the opportunity to submit comments on this proposed rule. The Board of Governors of the Federal Reserve System (the Board) proposes to amend Regulation Z to improve the effectiveness of consumer mortgage disclosures, clarify rescission rights, redefine "material disclosures" and rescission tolerances, and to require disclosures in connection with certain types of modified loans, among other things.

With this proposal, the Board continues its process of systematically creating improved TILA disclosures. We remain in support of clear, concise, informative disclosures because well-crafted disclosures will enable consumers to better understand the terms of their mortgage loans.

Need for Coordinated Rulemakings

As the Board was drafting its proposal, Congress enacted the Dodd-Frank Act (the DFA).[1] The DFA made a number of major changes to rules governing the financial services and mortgage finance industries, as well as the Truth in Lending Act (TILA), which Regulation Z implements.

As a result of DFA, some portions of the Board's current proposal need to be revisited. One mandate in the DFA is that the Real Estate procedures Act (RESPA) and TILA disclosures be integrated. This proposed rule contains a number of new disclosures that

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat 1376 (2010) (hereafter DFA).

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are not integrated with RESPA disclosures. Until that integration takes place, we believe the Board should not pursue changes to Regulation Z, and we urge that any Regulation Z changes be coordinated with the several upcoming DFA rulemakings. Furthermore, we strongly recommend that all disclosure revisions be done at one time, with appropriate testing and a rational implementation period. Making piecemeal, rather than coordinated changes to consumer disclosures would not provide any benefit to consumers, but it would impose a significant compliance and systems challenge to the industry.

Given that the Bureau of Consumer Financial Protection (the Bureau) has made the integration project an early priority, our recommendation seems prudent. In addition, we note that in one area the current proposal would create a new, and very serious, conflict with the RESPA rules that are now in force. The proposed rule would impose TILA liability for third party charges that RESPA rules do not permit creditors to control. We discuss the need to address and resolve this conflict below.

Finally, we recommend that federal policymakers working on the RESPA-TILA integration project begin by reviewing the enormous volume of work that has been already done in this area. More specifically, we would recommend that policymakers begin by using the TILA forms that the Board proposed in its 2009 rulemaking. While a few adjustments will need to be made to those forms, as we noted in our comment letter last year,[2] the forms are excellent. After making those adjustments, the information required by RESPA can be added to the Board's forms and the integration of the disclosures can be tested in a real-world environment and ultimately finalized.

Additional consumer information that describes the various types of mortgage products, settlement services, and the mortgage process itself should be prepared by a professional educational public relations firm that is experienced in using new media. In today's environment, many consumers simply do not read detailed handbooks. Instead, they "listen and watch." Recognizing this reality will help to ensure that consumers receive communications that enable them to understand and select the product choices that best meet their personal financial needs. The disclosure forms should not be used for general consumer education because that would crowd out the specific disclosures. Instead, the disclosure forms should be used to disclose to consumers the specific costs and terms of the mortgage options available to them and of the mortgage product they select.

Rescission Procedures

Notice of Right to Cancel

The Board proposes to revise the format and content of the notice of right to cancel. The content in the proposed notice is clearer because it presents information in a tabular format. We support this change.

[2] The Board's proposed TILA forms are excellent, but they will need to be expanded so they can be used smoothly in variable rate products. In addition, the industry does not have the capability to display the graphics that were proposed in the disclosure forms.

The Board also proposes to remove the antiquated requirement that creditors deliver two identical copies of the very same disclosure about the right to rescind. In the information age, this is a welcome improvement. It will help reduce information overload.

We recommend, however, that the Form H-8, Rescission Model Form (General) and H-9 Rescission Model Form (New Advance of Money With the Same Creditor) be combined into one. They differ only slightly, so they could be combined easily. The difference to consumers would be negligible because the key disclosure – the right to cancel and the deadline – would not differ. Yet operationally it would be substantially easier to comply because it would not require the creditor on the new loan to determine whether it is the original creditor.

We also recommend that the Board include a form for the notice of the right to cancel when an open-end loan finances the purchase of a home. The first advance would not be rescindable. However, future advances on the same line of credit would be. A form making this distinction clear to the consumer would improve consumer understanding.

Notice to Servicer

The Board proposes to permit a consumer to notify the loan's servicer of a rescission even if the servicer was not the original creditor. We support this change because the servicer is the entity with whom the consumer regularly communicates, not necessarily the original creditor. This intuitive process will make it easier for consumers to exercise their rights.

Important Clarity About Procedure for Rescission After Disbursement

We also support the Board's proposal concerning the procedure for rescissions after a creditor disburses loan funds. As currently written, Regulation Z could mislead consumers into believing that the mere execution and delivery of a rescission notice means the security interest becomes void, although this is not true. The Board's proposal would revise the regulation so that consumers would better be able to understand their right to rescind under Regulation Z.

Rescission is a remedy that restores the parties to their pre-contract position. That is, the creditor returns interest and other loan costs to the consumer, the consumer returns loan principal to the creditor, and the creditor records a release of its lien. In most cases, the net payment will be from the consumer to the creditor because the loan principal is a larger dollar amount than the interest and charges the consumer has paid on the loan.

Black's Law Dictionary defines the term "rescission" as follows:

> A party's unilateral unmaking of a contract for a legally sufficient reason, such as the other party's material breach, or a judgment rescinding the contract; Voidance. Rescission is generally available as a remedy or defense for a nondefaulting party and is accompanied by restitution of any partial performance, thus restoring the parties to their precontractual positions. Also termed avoidance.

TILA sets out the procedure for a rescission.

> When an obligor exercises his right to rescind under subsection (a) of this section, he is not liable for any finance or other charge, and any security interest given by the obligor, including any such interest arising by operation of law, becomes void upon such a rescission. Within 20 days after receipt of a notice of rescission, the creditor shall return to the obligor any money or property given as earnest money, downpayment, or otherwise, and shall take any action necessary or appropriate to reflect the termination of any security interest created under the transaction. If the creditor has delivered any property to the obligor, the obligor may retain possession of it. Upon the performance of the creditor's obligations under this section, the obligor shall tender the property to the creditor, except that if return of the property in kind would be impracticable or inequitable, the obligor shall tender its reasonable value.[3]

Many consumers do not understand the consequences of rescission and erroneously believe that delivery of an executed rescission notice immediately voids the lien without any need to return any principal. This is a serious misunderstanding.

TILA sets out the rights of the parties upon exercise of a "right" to rescind. Delivery of a rescission notice to a creditor may be an exercise of a "right" to rescind, but not necessarily. Not every loan is rescindable and not every executed rescission notice exercises a right to rescind. The Board's proposal merely provides time for a creditor to review the facts of the case and determine whether it believes there is a valid right to rescind. The proposal would make clear that TILA does not require any steps toward rescission based only on execution and delivery of a rescission notice. TILA requires those steps only after exercise of a *valid* right to rescind.

When there is a valid right to rescind, TILA provides that a rescinding obligor is not liable for any "finance or other charge[.]" At first glance, this may imply that the consumer has no further duty of any sort, but TILA also provides that a rescinding obligor "shall tender the property to the creditor" or tender "its reasonable value." That is, the language is seemingly contradictory, first stating that the rescinding obligor has no liability for charges, then requiring the consumer to repay the loan principal.

A closer reading clarifies the two phrases. Upon valid rescission, the obligor is no longer liable for "any finance or other charge" on the loan. A TILA "finance charge" includes interest and certain other, but not all, loan charges. The language that the obligor is not liable for any "finance or other charge" refers only to the interest and other loan charges. It does not cover the loan principal because, under TILA definitions, principal is not a "finance charge" or any type of "charge."

The phrase "the obligor shall tender the property" requires the obligor to return something, of course. It must refer to something the obligor could return. Loan principal

[3] TILA § 125(b), 15 U.S.C. § 1635(b).

is the only property the obligor would be able to return to a creditor because it is the only property the creditor has transferred to the obligor. Clearly, TILA requires rescinding borrowers to repay the loan principal.

The language making the creditor's security interest void upon a rescission does not require the creditor to release its lien immediately. Rather, within twenty days of receiving a valid notice of rescission, the creditor must take specified actions. Neither releasing its lien nor recording a release is among them. Within that period of time, the creditor must return earnest money and any downpayment. It must also take any action "necessary or appropriate" to reflect termination of its security interest. That is all the creditor is required to do.

It may not be "necessary or appropriate" for the creditor to release its lien immediately in all circumstances. Given that TILA requires a rescinding obligor to return the loan principal, it is only appropriate for creditor to release its lien when the obligor has met its obligation.

The Board's proposal is designed to clarify this statutory language and to implement the plain obligation of a rescinding obligor to repay the loan obligation.

Clarification Concerning Guarantors

The Board proposes helpful guidance about guarantors' rescission rights. The Board proposes a Comment that a right to rescind exists when guarantors both guarantee repayment and pledge their principal dwelling as security on a consumer credit transaction.[4] This is welcome clarity.

Clarification Concerning Estimated Dates

The Board proposes helpful guidance for circumstances in which creditors need to estimate the deadline for expiration of a right to cancel. The proposal permits estimates as necessary without affecting consumer's substantive rights. This is an appropriate clarification.

Rescission Waiver Requests

- *Investigation of Consumer's Personal Matters Should Not Be Required*

The Board proposes additional guidance about consumers' ability to waive the three-day rescission period so that a loan may fund upon consummation.

> The conditions for a waiver are not met where the consumer's waiver statement is inconsistent with facts known to the creditor.[5]

[4] Proposed Comment 2(a)(11)-1.i.
[5] Proposed Comment 23(e)2.iii.

It is unclear what is "inconsistent" with known facts. Is an implied possible difference inconsistent? How much inconsistency would be required? Creditors need either to permit or reject a waiver request, which requires a yes or no answer.

It is also unclear what a creditor "knows" because a creditor is a corporation. Upon receipt of a waiver request, does the Board intend the creditor to investigate the veracity of the request? If so, to what extent? How quickly? A reasonable inquiry could take much or all of the three days, and effectively eliminate all waivers.

If, for example, a consumer wishes a waiver to pay for emergency health care services, is the creditor to request and review medical information? Creditors are not medical experts, and will not be able to determine which medical services are needed immediately and which can wait. We also believe requiring consumers to provide detailed medical or other unneeded, but private information to creditors would be an unwarranted breach of privacy.

We do not believe creditors should be required to investigate the facts underlying waiver requests. Any investigation requirement would in effect eliminate all waivers.

- *Clarification About Consumer Facing Foreclosure*

We request clarification of one of the Board's examples of a *bona fide* personal emergency upon which a waiver is permissible. The Board proposes this example:

> The imminent sale of the consumer's home at foreclosure, where the foreclosure sale will proceed unless the loan proceeds are made available to the consumer during the rescission period.[6]

This could be read to imply that the consumer facing foreclosure must be the same consumer who is seeking a new loan and a waiver. One person may apply for a mortgage loan, on that person's home, to avoid foreclosure on a different consumer's home, such as to help a family member. We believe waiver should be permissible in this case.

Death of a Consumer

The Board proposes to incorporate into its regulation a clarification of a provision in TILA. This is the provision in TILA § 125(a) that a right to rescind a mortgage loan terminates upon transfer of all the consumer's interest in the property. The Board proposes to clarify that a consumer's death, which as a matter of law immediately transfers all the consumer's interest in all property, terminates that consumer's right to rescind. TILA mandates this outcome, and the clarification is helpful to consumers' understanding of their rights.

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[6] Proposed Comment 23(e)2.i.A.

Material Disclosures

The Board proposes a number of additions to, and deletions from, the definition of material disclosure. This definition is significant because a creditor's failure to deliver a required "material disclosure" extends the period during which a consumer may rescind a loan.[7]

> The Board now proposes to revise the definition of material disclosures to include the information that is critical to consumers in evaluating loan offers, and to remove information that consumers do not find to be important. The proposal is intended to ensure that consumers have the information they need to decide whether to rescind a loan.[8]

Overview of Proposed Changes to Material Disclosure

The Board proposes to remove from the definition of material disclosures the amount financed, the number of payments, and total of payments. This is designed to make the material disclosures be as their name conveys – disclosures of information that is material to consumers as they decide whether to rescind. The Board proposes to remove these items from the definition of material disclosure because consumer testing demonstrated that consumers do not place importance on the disclosures.[9]

The Board also proposes to exclude from the definition of material disclosures for reverse mortgage loans the loan amount, loan term, and payment summary. With reverse mortgage loans, the loan amount may be unknown, the loan term is unknown, and there are no periodic payments.

For reverse mortgage loans, the Board also proposes to exclude the loan features in proposed § 226.38(a)(ii) – step payments, payment options, and interest-only payments. These items are not relevant to reverse mortgage loans. The Board also proposes to exclude negative amortization as a material disclosure because there are no periodic payments, but would include the interest costs.

The Board proposes to add several items to the definition of material disclosures. It also proposes to revise the definition of "finance charge" to include more charges, including third party charges.

The Specific Proposed Changes

The Board proposes to define "material disclosures" to include a number of items, including the following:

For open-end loans:

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[7] Proposed § 226.15(a)(3)(ii) (open-end); § 226.23(a)(3)(ii) (closed-end).
[8] 75 Fed. Reg. 58539, 58613 (September 24, 2010).
[9] 75 Fed. Reg. 58539, 58619-20 (September 24, 2010).

- The annual percentage rate (the "APR").[10]
- The "total of all one-time fees imposed by the creditor and any third parties to open the plan disclosed under § 226.6(a)(2)(vii) or § 226.33(c)(7)(i)(A)[.]"[11]

For closed-end loans:

- The total settlement charges disclosed under § 226.38(a)(4) or the total fees under § 226.33(c)(7)(i)(A).[12] For this purpose, settlement charges are either of two amounts. One amount is settlement charges as disclosed under RESPA,[13] which includes third party settlement costs. (We discuss below a problem with using a RESPA reference for transactions not subject to RESPA.) The other amount is the total of all one-time fees, imposed by either a creditor or any third party, to consummate a reverse loan transaction, stated as a dollar amount.[14]
- The APR.[15]
- The interest and settlement charges disclosed under § 226.38(e)(5)(ii) or § 226.33(c)(14)(ii).[16]

The August 2009 closed-end proposal would add to the definition of finance charge certain third-party charges on closed-end loans, in § 226.4(g), and the Board has continued to include that § 226.4(g) with its current proposal.

As a result, the new definition of material disclosure, for both open-end and closed-end credit, would include third-party charges.

Modifications to Material Disclosure Should be Coordinated

The number of proposed changes to material disclosures alone increases the chances for inadvertent error, especially if there is not sufficient time to understand them and implement them properly.

We discuss below that the Board may not have fully considered the conflicts with RESPA. For this reason, we believe this rulemaking should be pursued only when it can be coordinated with the RESPA integration.

We also suggest that if the material disclosures were to be amended, revisiting the tolerances would be necessary.

Material Disclosures Should Not Include Third-Party Charges Without Addressing RESPA § 8

Including third-party charges in the definition of material disclosure creates a conflict

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[10] Proposed 12 C.F.R. § 226.15(a)(5)(i)(A).
[11] Proposed 12 C.F.R. § 226.15(a)(5)(i)(B).
[12] Proposed 12 C.F.R. § 226.23(a)(5)(i)(E).
[13] Proposed 12 C.F.R. § 226.23(a)(5)(i)(E), referring to § 226.38(a)(4).
[14] Proposed 12 C.F.R. § 226.23(a)(5)(i)(E), referring to 226.33(c)(7)(i)(A).
[15] Proposed 12 C.F.R. § 226.23(a)(5)(i)(G).
[16] Proposed 12 C.F.R. § 226.23(a)(5)(i)(I).

between RESPA and TILA rules, and this conflict creates a problem that needs to be resolved. The issue concerns settlement charges that the creditor cannot control because they are third-party charges. The reason the creditor cannot control those costs is not related to TILA, but is based on RESPA § 8. RESPA § 8, as currently implemented in Regulation X, does not permit creditors to control third party settlement costs, such as the charges for title examination and title insurance.

Not only can creditors not control those costs, creditors must rely on closing agents to tell the creditor what some of the costs are. This process is hardly infallible. A closing agent may permit charges to be added without the creditor's knowledge or approval.

Defining as a material disclosure the third party charges that the creditor cannot control and is not always able to know may extend a consumer's right to rescind a loan if the disclosure inaccurately states those charges. That is, it would very severely penalize a creditor for not controlling third party costs, while RESPA rules prohibit the creditor from doing just that. This is inappropriate, as well as unfair.

We understand the desire for consumers to have accurate disclosures of third party settlement costs, and agree with that goal. It is possible to have accurate disclosures while not penalizing creditors under TILA with the harsh remedy of rescission for complying with RESPA.

Several solutions to this problem are available.

- Exclude all third party charges for purposes of determining rescission tolerances.
- Provide ten percent tolerances for third-party charges, as under RESPA rules.
- Require disclosures of third party charges under RESPA but not under TILA.
- Relax RESPA § 8 liability for the purpose of improving consumer disclosures of third party settlement costs.
- Provide creditors with time after making a TILA disclosure to amend it to correct errors, much as RESPA rules permit 30 days after a loan closes to revise a settlement statement.[17]

We recommend consideration of this issue as RESPA disclosures are integrated with TILA disclosures. Until this issue can be resolved, we must oppose inclusion of third party settlement charges in the Regulation Z definition of material disclosure. This is unfortunate, because we believe the intent behind the Board's proposal, to ensure consumers know their settlement charges regardless of who provides the services, is in the interest of consumers.

Interest Rate and Payment Summary Should Not Be a Material Disclosure

Defining the Interest Rate and Payment Summary as a material disclosure would be inappropriate because the requirements for that disclosure are not always clear. On December 22, 2010, the Board revised the interim final rule that requires this disclosure

[17] 24 C.F.R. § 3500.8(c).

to clarify some matters, but uncertainty remains, as we will detail in a subsequent comment letter.

It would be fundamentally unfair to define as material any disclosure that the creditor in good faith may be unable to prepare accurately.

Defining Material Disclosures to Include Settlement Disclosures Disclosed Under RESPA

The proposal would define material disclosures to include settlement charges as disclosed under RESPA on certain closed-end transactions. The Board also proposes to require Regulation Z disclosures on modifications that are not subject to RESPA. For transactions not subject to RESPA, this reference would need revision.

This presents yet another example of the need to coordinate TILA disclosures with RESPA disclosures rather than pursue them independently.

Refinance with the "Same Creditor"

TILA permits consumers to rescind loans in some, but not all, circumstances. It exempts from rescission:

> [A] transaction which constitutes a refinancing or consolidation (with no new advances) of the principal balance then due and any accrued and unpaid finance charges of an existing extension of credit by the same creditor secured by an interest in the same property[.][18]

When an existing loan is refinanced, it can be unclear whether the "same creditor" is making the change to the loan. The Board proposes that an extended right to rescind a loan terminates when the loan is refinanced, if the refinanced loan is made by a creditor other than the current holder.[19] It also proposes that rescission rights should not apply to a loan refinanced by the same creditor, and proposes to define "same creditor" to mean the original creditor, to whom the loan was initially payable, if that creditor is also the current holder of the loan.[20]

We believe that in a refinance the right of rescission for the new loan should apply only to new advances. Any redress regarding the prior loan should be pursued against the creditor that made the prior loan, not the creditor who makes the new loan.

A hypothetical example will illustrate why this distinction is appropriate. Creditor A makes a loan and fails to deliver a required material disclosure. Creditor A sells the loan to Creditor B within three years. Also within three years, the consumer refinances the loan that Creditor B owns with Creditor A, the creditor at fault. Creditor A has already

[18] TILA § 125(e)(2).
[19] Proposed § 226.23(a)(3)(ii).
[20] Proposed § 226.23(f)(2)(i).

been repaid for the original loan by selling the loan to Creditor B. Under the proposal, this refinance would terminate the consumer's right to rescind the original loan. This is contrary to the Board's stated intent of preventing "unscrupulous creditors [from] refinanc[ing] their own loans . . . to purposely terminate a consumer's right to rescind the previous loan[.]"[21]

The Board's proposal would effectively rewrite TILA. TILA plainly exempts refinanced loans from rescissions to the extent there are no new advances. Congress just passed a law that rewrote and revised much of TILA, yet Congress left alone the language quoted above.

We recommend that the Board limit the rescission of the refinanced loan to the extent of new advances, as Congress requires. This does not need to affect any rights the consumer may have as to the original creditor on the original loan. In the example above, even after refinancing, the consumer would remain able to seek redress from Creditor A, the creditor at fault on the earlier loan, for the failure to deliver material disclosures for that loan, but not from Creditor B, the creditor not at fault. This would be more equitable than penalizing Creditor B and not Creditor A for Creditor A's violation.

Rescission Tolerances

Having proposed to redefine material disclosures, the Board also proposes to revise the tolerances, for rescission purposes, to cover the newly defined material disclosures. The Board explains:

> The Board recognizes that increasing the number of material disclosures could increase the possibility of errors resulting in extended rescission rights. Although the creditor must re-disclose any changed terms before consummation, consistent with § 226.17(f), there may still be errors in the final TILA disclosure. To ensure that inconsequential disclosure errors do not result in extended rescission rights, the Board proposes to add tolerances for accuracy of disclosures of the loan amount, the total settlement charges, the prepayment penalty, and the payment summary. The proposal would retain the existing tolerances for the interest and settlement charges (currently referred to as the "finance charge").[22]

We understand the intent behind the proposal, but we explain why it cannot work as intended. First, we set out the proposed tolerances:

Tolerances for Rescission Purposes – Open-End

For open-end credit, the proposal would set a tolerance for rescission purposes for the total of all one-time fees to open the plan that are imposed by the creditor and by third parties, and other disclosures affected by the total. The disclosure would be considered accurate if it were understated by no more than $100, and overstatements would be

[21] 75 Fed. Reg. 58539, 58612 (September 24, 2010).
[22] 75 Fed. Reg. 58539, 58614 (September 24, 2010).

considered accurate.[23]

Tolerances for Rescission Purposes – Closed-End

For closed-end credit, the proposal would set tolerances, for rescission purposes, as follows.

- *Interest and Settlement Charges, and APR*

Disclosures of the interest and settlement charges and of the APR, with two exceptions, would be considered accurate if they were understated by no more than one half of one percent of the note amount, or $100, whichever is greater. In the case of a refinance with a new creditor without a new advance or loan consolidation, the disclosure would be considered accurate if it were understated by no more than 1% of the note amount or $100, whichever is greater. After foreclosure is initiated on a consumer's principal dwelling, the disclosure would be considered accurate if it were understated by no more than $35. In each case, an overstatement would be considered accurate.[24]

- *Loan Amount*

The disclosed loan amount would be considered accurate, with two exceptions, if it were understated by no more than as one half of one percent of the note amount or $100, whichever is greater. In the case of a refinance with a new creditor without a new advance or loan consolidation, the amount disclosed would be considered accurate if it were understated by no more than 1 percent of the note amount or $100, whichever is greater. In each case, an overstatement would be considered accurate.[25]

- *Total Settlement Charges, Prepayment Penalties, and Payment Summary*

A disclosure of total settlement charges, prepayment penalties, and payment summary would be considered accurate if each disclosure were understated by no more than $100, and overstatements would be considered accurate.[26]

- *Loan Term*

The Board does not propose, but requests comment on, whether it should include a tolerance for the loan term. We recommend that the tolerance be sufficient to accommodate the difficulty in defining the loan term precisely in disclosures prepared more than three days before consummation, so that creditors making disclosures in good faith will not exceed the tolerances.

[23] Proposed 12 C.F.R. § 226.15(a)(5)(ii).
[24] Proposed 12 C.F.R. § 226.23(a)(5)(ii).
[25] Proposed 12 C.F.R. § 226.23(a)(5)(iii).
[26] Proposed 12 C.F.R. § 226.23(a)(5)(iv).

Tolerances for Rescission Purposes Should Bear a Relation to the Amount of Consumer Harm and to the Severity of the Rescission Penalty

The Board has proposed a number of new tolerances for rescission purposes. Many of them are quite low, often only $100, and one is only $35. The Board describes how it arrived at its proposed tolerances. "[T]his proposal would provide a tolerance for the loan amount modeled after the tolerances for the finance charge created by Congress in 1995."[27]

We question why this is appropriate in light of the significant changes the proposal would make to the finance charge, to be called the interest and settlement charge. In particular, this proposal would include third party charges in the definition of finance charge, and subject the creditor to a minor tolerance for charges the creditor cannot control.

At the time Congress created the tolerances, the finance charge excluded items that the Board would now include, including third party charges. It simply does not follow that the tolerances for material disclosures should remain at the same level while the definition of material disclosures is greatly expanded.

Especially where a tolerance can be as low as $35 – an amount that may not even increase with inflation – rescission would be an extraordinarily harsh penalty, wholly disproportional to any consumer harm, and wholly disproportional to the damage to creditors.

The Board states that the purpose of its proposal is "to ensure that consumers have the information they need to decide whether to rescind a loan."[28] We respectfully suggest that rescinding a loan over $100 or $35 is most unreasonable. If the problem were that a consumer was inappropriately charged a small amount of money, rescission would be an inappropriate remedy because it is disproportional to the amount of consumer harm.

The Board states that its intention is "[t]o ensure that inconsequential disclosure errors do not result in extended rescission rights,"[29] but the effect would be to ensure that inconsequential errors *do* extend rescission rights.

If creditors were subject to the harsh penalty of rescission under miniscule tolerances, a few inadvertent inaccuracies that the creditor cannot prevent due to RESPA § 8, that have only a negligible effect on consumers, could put creditors, especially small creditors, out of business. We strongly urge the Board to rethink the level of the rescission tolerances.

Tolerances and Inflation

The Board also asks whether it should adjust the loan amount tolerance figure of $100, which was set in 1995, or adjust it for inflation. We believe all tolerances that are set as a

[27] 75 Fed. Reg. 58539, 58615 (September 24, 2010).
[28] 75 Fed. Reg. 58539, 58613 (September 24, 2010).
[29] 75 Fed. Reg. 58539, 58614 (September 24, 2010).

fixed dollar amount should be adjusted for inflation because over time inflation can have a significant effect. We do not believe this should require a rulemaking for each adjustment because it would be a mere arithmetic calculation. Just as the Board annually adjusts its HOEPA points and fees threshold under § 226.32(a)(1)(ii) without a notice and comment rulemaking, it should do the same for this tolerance. Given that the $100 figure has not been adjusted for inflation since 1995, the first adjustment should account for inflation since that year.

The Board did not propose a different tolerance for the loan amount in connection with a foreclosure, due to compliance concerns. We share the Board's concern about compliance. TILA compliance is one of the most difficult areas of compliance in consumer mortgage lending, and it imposes tremendous costs on creditors. Consumers in the long run bear all those costs. To the extent that a reasonable tolerance can reduce the cost of housing credit, it would benefit consumers and the housing markets.

The Board also solicits comment on whether the loan amount tolerance should be revised to be similar to the HOEPA tolerance, under which a disclosure is considered accurate if it is overstated or understated by no more than $100. We believe this would be inappropriate. It is understandable that Congress put extra restrictions on HOEPA loans. HOEPA loans are a narrow and specific category of loans warranting specialized restrictions. It does not follow that the same restrictions should apply to all loans.

Additionally, creditors are under strong competitive pressure not to overstate the loan amount because that would risk overstating other amounts that are tied to the loan amount, and that could drive a promising customer to the creditor's competitor.

For these reasons, we believe the loan amount tolerance, and all tolerances expressed as a fixed dollar amount, should adjust for inflation.

Disclosures in Connection With Loan Modifications

The Board's proposal would require new disclosures in some but not all instances when the same creditor and consumer modify an existing loan obligation, which the Board would define as a new transaction.

A modification of an existing loan is not the origination of a new loan transaction. It merely revises one or a few terms of an existing loan. It does not require releasing a lien and replacing it with a new one because the same loan is in place before and after the modification. There is no new loan transaction. Despite the fact that there is no origination of a new loan, the Board is proposing to require a full set of TILA origination disclosures, with all of the inherent complexities, all of the TILA liability and litigation risk, a three-day waiting period, and a right to rescind. This would be very disproportionate to the modification, a relatively simple event with low risk to consumers. A clear, concise, complete disclosure for modifications could fit on one page. A modification disclosure should not be complicated, much like a rate reset notice.

Moreover, modifications can be beneficial to consumers. A common type of modification, other than one in connection with default or imminent default which we discuss below, is the conversion of an adjustable rate to a fixed rate when interest rates are rising. This is beneficial to the creditor who retains a customer considering refinancing with a different creditor. It benefits the consumer who can avoid a rate increase and avoid the cost of a refinance. There is no need for a full array of disclosures for such a minor and beneficial change. Another common type of modification is a loan assumption. In this case, no loan term changes. Any disclosure in connection with modifications should be tailored to just the information that is relevant to a modification.

Were the Board to require a full array of disclosures for modifications, it would not inform consumers about the terms of the modification. It would greatly reduce the possibility of modifications.

Default or Delinquency

The Board's proposal would not require new disclosures for a modification in connection with a default or delinquency, unless there is an increase in the loan amount, an increase in the interest rate, or unless the creditor imposes a fee for the modification. The Board solicits comment on whether, for modifications in the case of default or delinquency, to require a new, streamlined disclosure that highlights changed terms, or whether to keep the proposed exception from modification disclosures in cases of default or delinquency.

We believe it is important for consumers to understand their loan terms in all circumstances. We believe, though, applying TILA to modifications in the event of default or delinquency would be very harmful.

It is important for policy makers to understand that adding new TILA litigation risks onto loan modifications would increase the cost, and therefore reduce the availability of, loan modifications.

Done correctly, modifications in the event of default can provide a benefit to consumers and to the communities in which they live. The Treasury Department has made its Making Home Affordable programs, HAMP and HARP, a central part of its response to the housing crisis. FHA has adopted an analogous modification program for the same reasons. Loan servicers also have adopted similar modification programs. Imposing TILA liability on these modification programs could eliminate them overnight.

To the extent that the Board can identify a shortcoming in disclosures used in modifications in case of default, it could ask Treasury to incorporate new disclosures into its HAMP and HARP programs, and FHA into its program, rather then to require them under TILA.

This approach would not be limited to HAMP, HARP, and FHA programs. Rather, this approach would smoothly incorporate the same disclosures into modifications performed outside of the Treasury's programs because Congress enacted a "servicer safe harbor" against liability for servicers that use modification programs, such as the Treasury's programs.[30] In this way, the Board could cause creditors to use the disclosures it believes are best without causing the risk of TILA liability to disrupt a major platform of the country's foreclosure prevention efforts.

Imminent Default

The Board also solicits comment on whether consumers should be provided TILA disclosures when they are in imminent default or delinquency. The Treasury's HAMP and HARP programs are specifically designed to avoid foreclosure for borrowers who are in imminent default. This is a central platform of the Treasury's housing policies. We do not believe TILA litigation risk should be imposed because it would severely disrupt Treasury's policies and programs, as well as the housing markets.

We recommend that the Board include an exception to the proposed new disclosure requirement in proposed § 226.20(a)(1)(ii) for "Modifications, including trial period plans and refinances, consistent with the Home Affordable Modification Program and the Home Affordable Refinance Program established by the Department of the Treasury."

Clarification on the definition of imminent default would be advisable. The HAMP guidance provides:

> A borrower that is current or has only one payment due and unpaid by the end of the month in which it is due and who contacts the servicer to request HAMP consideration must be evaluated to determine if he or she is at risk of imminent default. Each servicer must have written standards for determining imminent

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[30] (a) IN GENERAL.—Notwithstanding any other provision of law, whenever a servicer of residential mortgages agrees to enter into a qualified loss mitigation plan with respect to 1 or more residential mortgages originated before the date of enactment of the Helping Families Save Their Homes Act of 2009, including mortgages held in a securitization or other investment vehicle—
(1) to the extent that the servicer owes a duty to investors or other parties to maximize the net present value of such mortgages, the duty shall be construed to apply to all such investors and parties, and not to any individual party or group of parties; and
(2) the servicer shall be deemed to have satisfied the duty set forth in paragraph (1) if, before December 31, 2012, the servicer implements a qualified loss mitigation plan that meets the following criteria:
(A) Default on the payment of such mortgage has occurred, is imminent, or is reasonably foreseeable, as such terms are defined by guidelines issued by the Secretary of the Treasury or his designee under the Emergency Economic Stabilization Act of 2008.
(B) The mortgagor occupies the property securing the mortgage as his or her principal residence.
(C) The servicer reasonably determined, consistent with the guidelines issued by the Secretary of the Treasury or his designee, that the application of such qualified loss mitigation plan to a mortgage or class of mortgages will likely provide an anticipated recovery on the outstanding principal mortgage debt that will exceed the anticipated recovery through foreclosures.
(b) NO LIABILITY.—A servicer that is deemed to be acting in the best interests of all investors or other parties under this section shall not be liable to any party who is owed a duty under subsection (a)(1), and shall not be subject to any injunction, stay, or other equitable relief to such party, based solely upon the implementation by the servicer of a qualified loss mitigation plan.
Preventing Mortgage Foreclosures And Enhancing Mortgage Credit, Pub. L. No. 111-22, § 201, 123 Stat. 1632, 1638-39 (2009).

> default that are consistent with applicable contractual agreements and accounting standards and must apply the standards equally to all borrowers.[31]

Any TILA definition of imminent default should be consistent with the HAMP definition because this definition is in widespread use and is designed specifically to benefit consumers.

Clarification of Creditor Under HARP

We request one clarification concerning the identity of the creditor under the HARP program. Under this program, the government sponsored entities Fannie Mae and Freddie Mac (the GSEs) refinance loans for eligible borrowers. Each GSE may only refinance loans that it owns or has guaranteed through its mortgage-backed securities.

Fannie Mae and Freddie Mac are both prohibited by their charter acts from originating loans.[32] They both also are generally prohibited from acquiring loans with a loan-to-value ratio greater than 80 percent without credit protection, usually mortgage insurance.[33] Further, both are required to obtain regulatory approval before offering new products. Regulatory approval is not permitted before public notice and opportunity to comment.[34]

To effectuate HARP, the Federal Housing Finance Agency (FHFA) conditionally approved GSE participation as "akin to a loan modification for charter purposes" rather than as a loan without required mortgage insurance.[35] FHFA noted the "unusual and exigent market circumstances" and did not enforce the prohibition on GSE loan origination, and did not enforce the required public notice-and-comment procedure for new GSE products.[36]

The Board discusses the definition of creditor for purposes of proposed § 226.20(a)(1):

> The Board believes that any person who makes significant changes to the terms of an existing legal obligation, such as the interest rate or the loan amount, engages in extending credit to the consumer by continuing the extension of debt on different terms and, therefore, is a "creditor" under TILA.[37]

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[31] *Making Home Affordable Program Handbook for Servicers of Non-GSE Mortgages*, version 3.0, § 4.4, p. 58 (December 2, 2010), available here https://www.hmpadmin.com/portal/programs/docs/hamp_servicer/mhahandbook_30.pdf

[32] Fannie Mae charter § 304(a)(2)(B), 12 U.S.C. § 1719(a)(2)(B); Freddie Mac charter § 305(a)(5)(B), 12 U.S.C. § 1454(a)(5)(b).

[33] Fannie Mae charter § 302(b)(2), 12 U.S.C. § 1717(b)(2); Freddie Mac charter § 305(a)(2)(C), 12 U.S.C. § 1454(a)(2)(C).

[34] Housing and Economic Recovery Act of 2008, § 1123, Pub. L. No. 110-289, 122 Stat 2654, 2689 (to be codified at 12 U.S.C. § 4541).

[35] Letter from James B. Lockhart III, Director, FHFA, to Suzanne Hutchison, Executive Vice President, Mortgage Insurance Companies of America (February 20, 2009), available at: http://www.fhfa.gov/webfiles/1256/HutchinsonGSERefi22009.pdf

[36] *Id*.

[37] 75 Fed. Reg. 58539, 58597 (September 24, 2010).

We request clarification of the definition of creditor when a GSE refinances a loan under HARP.

We also suggest that the difficulty of the many issues surrounding this question provides further reason not to apply proposed § 226.20(a)(1) to the Treasury Department's HAMP and HARP initiatives due to unintended consequences. Requiring TILA disclosures for HAMP and HARP would have a number of unforeseen and unintended consequences such as this one. Of course, crippling HAMP and HARP would be another consequence.

Clarification of Creditor Outside of HARP

It is not entirely clear in a modification who the creditor would be for disclosure purposes. Logically, it would seem to be the holder of the obligation, but identifying this holder in TILA disclosures would be quite confusing to consumers. Identification of the servicer would be more relevant, as the Board recognizes in its proposal to permit consumers send cancellation notices to servicers. We request clarification that the "creditor" for modification disclosures would be the servicer, even though the servicer is not the creditor for other TILA purposes.

Increase in Loan Amount

New disclosures would be required when a modification increases the loan amount. The Board asks whether it should establish a *de minimis* threshold for increased loan amounts below which disclosures should not be required. This would be appropriate because without a minimum threshold, creditors will not make minor changes due to TILA litigation risk. For example, a consumer with a HELOC may inadvertently go over the credit limit by a small amount. This should not require a disclosure under § 226.20.

Determining the loan amount on a modification is difficult because the loan amount can change daily as interest accrues and as a consumer makes payments. When preparing a disclosure, the creditor may not know the date the modification will become effective, and will not know the loan amount.

We recommend that the Board permit the creditor to prepare disclosures based on an assumption that the modification will be effective on a scheduled payment date, and that all payments will be made when and in the amounts scheduled.

Definition of Application

The Board proposes to require disclosures within three days after a consumer applies for a modification. It proposes to incorporate the RESPA definition of application.

> Creditors may rely on RESPA and Regulation X (including any interpretations issued by HUD) in deciding whether a "written application" has been received. In general, Regulation X defines an "application" to mean the submission of a

> borrower's financial information in anticipation of a credit decision relating to a federally-related mortgage loan, using the RESPA definition of application.[38]

The use of common definitions under RESPA and TILA rules would normally be a welcome integration of the two areas of rules. Nevertheless, in this matter, we believe the RESPA definition of application needs clarification. The RESPA definition is:

> *Application* means the submission of a borrower's financial information in anticipation of a credit decision relating to a federally related mortgage loan, which shall include the borrower's name, the borrower's monthly income, the borrower's social security number to obtain a credit report, the property address, an estimate of the value of the property, the mortgage loan amount sought, and any other information deemed necessary by the loan originator.[39]

- *Would a Submission Be Required?*

The Board proposes to permit creditors to rely on information they already have on file for modifications.

> The Board is aware that consumers may not always formally apply for a modification of the terms of an existing obligation. In many cases, the creditor may have in its possession the information in the definition of "application" under RESPA and Regulation X (*e.g.,* the consumer's name, monthly income, or property address). *See* 12 CFR 3500.2(b). Therefore, proposed comment 20(a)(1)(i)–4 also provides that an application is deemed received in those instances where the creditor has the information necessary to constitute an "application" as defined under RESPA and Regulation X, whether the creditor requests the information from the consumer anew or uses information on file.[40]

This seems to contradict the RESPA definition, which requires "the **submission** of a borrower's financial information." If the creditor were to use information already on file, it would not have the submission necessary for a RESPA-defined application.

We request clarification that the income information and property valuation on which a creditor relies must be current at the time of a modification. Income and property values can fluctuate in a short amount of time, so that the information collected during origination likely will be obsolete at the time of a modification.

- *What Information Would Be Required?*

The RESPA definition permits loan originators flexibility to decide what they require in loan applications. Could a creditor use one definition of application for RESPA purposes

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[38] Proposed Comment 19(a)(1)(i)-2.
[39] 24 C.F.R. § 3500.2(b).
[40] 75 Fed. Reg. 58539, 58598 (September 24, 2010).

and a different one for modification purposes? This is not clear because the RESPA definition is not designed to answer that question.

Moreover, the RESPA definition is designed for a full loan application, which may be much different from the Board's broad definition of modification. Must the creditor require "the borrower's social security number to obtain a credit report" for every modification? The Board seems to want creditors not to charge fees for modifications, but requiring credit histories would appear to counter that goal. Using the RESPA definition of application, creditors will be compelled to obtain credit histories for every modification.

By the same reasoning, creditors will feel compelled to obtain "an estimate of the value of the property" for every modification. In many instances, this would be an expense for no apparent purpose. Further, the DFA will require new regulations for automated valuation methods, which will increase their costs.[41] Valuations should be current when creditors rely on them, but it does not follow that creditors must use them for every modification broadly defined.

- *What Would Trigger a Disclosure?*

If the definition were clarified to permit creditors to use information on file, what would trigger the disclosure? One proposed comment would provide that the modification disclosure requirement would arise when the creditor "has" the information enumerated in the RESPA definition.

> Whether the creditor requests the information from the consumer anew or uses information on file, an application is deemed received where the creditor has the information set forth in the definition of "application" as defined under Regulation X.[42]

It is not clear what it means for a corporation to "have" information. Does the three-day period begin when the consumer calls and asks for a modification? Or is the creditor permitted time to determine whether it has sufficient information, that is recent enough, before the three-day period begins?

When the consumer first indicates a possible desire for a modification, it is in many cases not clear what type of transaction would be appropriate under the circumstances. This determination must precede the determination whether the creditor has sufficient information to consider the modification.

We are concerned that the definition of application would require disclosures, with attendant TILA litigation risk, within three days of a consumer phone call, from a consumer who may not be audible or who may not speak English, which might be construed as a request for some unspecified modification. Under a vague definition,

[41] DFA § 1473(q), 24 Stat 1376, 2198 (2010).
[42] Proposed Comment 20(a)(1)(i)-4.

creditors would have only two choices. First, avoid modifications. Second, require formal, written applications specifying the type of modification requested, so creditors can be certain when the three day period begins to run, and can have some factual basis upon which to prepare a disclosure.

Lender-Placed Insurance

The Board proposes not to require disclosures when insurance coverage is extended.

> Charging an insurance premium for the continuation of coverage does not constitute a fee under § 226.20(a)(1)(i). That is, if a creditor does not impose on the consumer additional insurance premiums or new insurance requirements (for example, if the creditor does not increase the existing premium for hazard insurance or require increased property insurance amounts), but merely continues coverage, such costs are not fees imposed on the consumer in connection with the agreement under § 226.20(a)(1)(i).[43]

This language could be read to require a new disclosure when a servicer places hazard insurance after a consumer fails to purchase the required insurance, or the required amount of insurance, if the premium increases. There is already a series of rules for lender-placed insurance, and the Dodd-Frank Act rules may revise them.[44] To the extent those disclosures are insufficient, they should be revised.

We request clarification that proposed § 226.20 does not apply to lender-placed insurance because the need for a lender to place insurance only arises when a consumer fails to purchase insurance as required, and is therefore in default, under proposed § 226.20(a)(ii)(B). This need for a § 226.20 disclosure in connection with lender-placed insurance would need to be revisited if § 226.20(a)(1) were made applicable to instances of default to ensure it would not require a disclosure that it not consistent with the existing disclosures for lender-placed insurance.

Payment Decreases Do Not Need Disclosures

The Board asks whether disclosures should be required when a payment decreases.

> The Board solicits comment on whether consumers would benefit from having new TILA disclosures not only for increases in the periodic payment amount, but also for decreases in the payment amount obligation, when no other terms listed in § 226.20(a)(1)(i)(A)–(G) are modified.[45]

Consumers do not need protection from events that benefit them. Requiring TILA disclosures would harm consumers more that it would help them. Increasing TILA litigation risk in these cases would deter creditors from taking actions that would lower

[43] 75 Fed. Reg. 58539, 58762 (September 24, 2010).
[44] TILA § 129D(j)(2)(C), added by DFA § 1462, 24 Stat 1376, 2181-82 (2010).
[45] 75 Fed. Reg. 58539, 58600 (September 24, 2010).

payment obligations, which is contrary to the Board's goals. As the Board similarly reasons:

> The Board believes that where creditors provide these consumers [in default] with certain changes to terms, such as a decrease in rate and payment, and the consumer does not take on new debt or pay any fee, the modification is beneficial. In these instances, the benefit to consumers of a TILA disclosure appears outweighed by the risk that creditors would be discouraged from extending beneficial modifications (in lieu of foreclosure) due to the burden of giving new TILA disclosures and the potential exposure to TILA remedies for errors, including rescission.[46]

The Board's proposal would not require new disclosures when the only change to a loan is a rate decrease. We also recommend that no disclosure should be required when the payment amount is lowered. We request clarification that disclosure also would not be required where an adjustable rate mortgage loan (ARM) is modified to a fixed rate but there is no rate change.

Creditors should not be discouraged by TILA risks from lowering loan rates or payment amounts, or from converting ARMs to fixed-rate loans.

Term Extension and Reamortization to Lower a Payment Should Not Require Disclosure

Proposed § 226.20 exempts from the disclosure requirement a rate decrease with no other modifications except a decreased payment amount or term extension, or both, with no fee. This should be amended to permit the creditor to reamortize the loan over the extended term and increase the number of payments. We recommend that no modification disclosure be required in this case as long as there is no prepayment penalty.

ARM Converting to Fixed-Rate Loan Pursuant to Original Agreement

The Board solicits comment on whether, when an ARM is converted to a fixed-rate loan pursuant to its existing legal obligation, new TILA disclosures under § 226.20(a) should be provided instead of notice of an interest rate adjustment under § 226.20(c).[47]

The § 226.20(c) disclosures of rate adjustment would be required when a fixed rate loan converts, under its contract, to an ARM. The disclosure would be in the format of Form H-4(G) or (K). These form disclosures are designed to provide all the relevant information, in clear language, in a format that is easy to read. To the extent the Board believes there is a deficiency with these forms, the Board could revise them.

The Board asks whether liability risk, including rescission risk, of requiring disclosures under § 226.20(a), would discourage creditors from providing ARMs that convert to

[46] 75 Fed. Reg. 58539, 58601 (September 24, 2010).
[47] 75 Fed. Reg. 58539, 58606 (September 24, 2010).

fixed-rate loans.[48] TILA liability can be so severe that it always discourages creditors from offering products subject to that risk.

Proposed Comment 20(c)-4 suggests that a disclosure would be required when an ARM converts to a fixed rate and there is a conversion fee, even if the existing obligation provides for the option by specifying the index and margin used to calculate the fixed rate and by specifying that there will be a fee. We do not believe disclosure should be required in this circumstance because, from the consumer's point of view, the conversion is easy to understand. From the creditor's point of view, the conversion entails significant costs, so that a fee is reasonable. Any new restriction on conversion fees should not apply to contracts existing before a new rule becomes effective.

Rate Determination on ARMs

The Board proposes a comment to clarify how to determine whether there is a rate change on an ARM.

> A change in rate occurs for purposes of § 226.20(a)(1)(i)(D) when the interest rate (the fully-indexed rate for an adjustable-rate mortgage) for the new obligation is different than the interest rate for the existing obligation that is in effect within a reasonable period of time of the modification. For example, 30 calendar days would be a reasonable period of time.[49]

We request additional clarity for certain situations.

The initial rate on the modification may be higher or lower than the fully-indexed rate. If the new fully-indexed rate is the same as the current rate on the existing obligation, are disclosures required? The initial rate on the modification may not be the same as the rate on the existing obligation in this instance.

The existing obligation may be an ARM. If so, in almost all cases, its current rate will not equal the fully-indexed rate computed using a recent index value, either because the initial rate was not set using the index or margin or because the index value has changed since the loan was made or last adjusted. Should creditors use the current rate or the fully-indexed rate? If the fully-indexed rate, what index value should be used?

We appreciate the proposed use of a reasonable time as a way to ease compliance. However, we do request clarity. If the rate on a current obligation is 4 % and will increase in less than 30 days to 5%, and the rate on the modification will be fixed at 5%, are disclosures required because one of the rates in effect during the 30 days differs from the rate on the new obligation?

If not, then the 30-day example will need to be coordinated with section 1418 of the DFA. This will require notices six months before a rate reset. This notice will be

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[48] 75 Fed. Reg. 58539, 58606 (September 24, 2010).
[49] Proposed Comment 20(a)(1)(i)(D).

required to list alternatives the consumer may pursue, including a renegotiation of loan terms, that is, a modification. We suggest that if the rate on the existing obligation would increase within six months, modification to a rate less than or equal to the rate in the DFA reset notice should not be considered a rate increase. This would harmonize and streamline the disclosures and thereby improve consumer understanding.

Removal of Risky Features

The proposal would require disclosures if a modification would add new features such as an adjustable rate, prepayment penalty, interest-only payments, negative amortization, balloon payment, demand feature, no- or low-documentation, or shared equity or appreciation. By the same reasoning, we suggest that removal of any of those features should not by itself require a disclosure.

Modification Fees

We recommend that creditors be permitted to charge reasonable modification fees without requiring disclosures. Modifications do impose costs on creditors. When a consumer seeks a modification, creditors will weigh the modification against requiring a refinance. Without the ability to collect a modification fee, refinance will be required more frequently. Especially when market rates are rising or have risen, this can harm consumers. We believe that $500 would be a reasonable modification fee.

Accrued Interest

We request clarification about how to reflect accrued unpaid interest in calculating prepaid finance charges, the amount financed, total of payments, APR, and other disclosures. Should the disclosures include accrued interest and be calculated in the same manner as current Comment 226.20(b)-6? Including accrued interest in the disclosed loan amount would greatly complicate preparing disclosures because the amount of accrued interest makes the loan amount change on a daily basis. The difference to consumers would not be significant because the consumer is already aware that the loan accrues interest. We recommend that creditors be explicitly permitted to make modifications effective on a payment due date and to prepare final disclosures based upon the assumption that the loan will be current on that date.

Three-Day Refundable Fees

The Board proposes to permit consumers with a right to a refund of most fees imposed during the three business days following the consumer's receipt of early disclosures, for closed-end loans secured by real property or a dwelling.[50]

RESPA rules have no such requirement. Similar to Regulation Z, Regulation X requires a disclosure within three days of loan application, and prohibits charging a fee, other than

[50] Proposed § 226.5b(e) (open-end); proposed § 226.19(a)(1)(iv) (closed-end).

for a credit history or credit report, until after the applicant has received a GFE.[51] HUD has advised, in Frequently Asked Questions, that no fee is permissible until after the consumer has received a GFE and has "indicate[d] an intention to proceed with the loan[.]"[52] The RESPA FAQs did not go through notice-and-comment rulemaking, so they are not binding law.

We believe RESPA and TILA rules should be consistent about when a creditor or loan originator may charge a fee. This is one area where there is no statutory or other reason why the rules should differ. Having a uniform standard would provide uniform treatment to consumers, regulatory clarity, and would ease compliance costs.

We recommend that a creditor be permitted to charge the consumer at the earlier of either the consumer's expression of an intention to proceed or the end of three days. The early disclosure should make clear when a consumer will be charged and the amount. This way, consumers will be permitted to make informed choices about their loan's progress.

We request clarification about the refundability of counseling fees. Counselors may provide their services before a consumer decides to apply for a loan or selects a creditor. Counseling fees in advance of a loan application should not be refundable, regardless of whether the fee is required by law.

Portions of the Board's Proposal Will Not Survive the DFA

Clearly, the Board has put considerable effort into the current, very lengthy proposal. While the Board was working on this proposal, Congress passed the DFA. The DFA will change the laws governing consumer mortgage loans, as well as the TILA disclosures. We believe the timing of the Board's proposed rule and of the imminent DFA rulemakings warrants consideration.

The DFA rulemakings are already underway. Treasury has suggested that the new Bureau may propose new regulations before the designated transfer date. In this case, final Dodd-Frank rules could become final on or soon after the designated transfer date, which is only seven months away.

The DFA rules will revise many of the provisions in this proposed rule. We question whether it is appropriate to continue with the present rulemaking. A final rule resulting from the present proposal would have a very short life. The mortgage industry would need to incur the costs of complying with the new rule, and immediately thereafter, undo implementation of the new rule and begin implementing the DFA rules. We believe this would be counterproductive. We address the extent of the regulatory burden later in this letter. Here we question the need for it.

[51] 24 C.F.R. § 3500.7(a), (b).
[52] *New RESPA Rule FAQs*, p. 7, no. 10 (April 2, 2010).

Rather than continue with the present rulemaking, we urge the Board to incorporate its changes into the DFA rulemakings, including the integration of RESPA disclosures into the TILA disclosures.

Transaction Coverage Rate

In its August 2009 closed-end proposal, the Board proposed an "all-in APR" to more accurately reflect the cost of mortgage credit. This would have amended the definition of "finance charge" to include certain third-party charges. In our comment letter in response to that proposal, we supported the concept behind the proposal. However, we noted that the proposal would result in one unintended consequence, causing prime loans to reach the thresholds for loans governed by the Home Ownership and Equity Protection Act of 1994 (HOEPA) loans and for higher-price mortgage loans (HPMLs) restricted under Regulation Z § 226.35.

The current proposal revises the August 2009 closed-end proposal to define HPMLs by a "transaction coverage rate" (TCR) to prevent prime loans from reaching the thresholds designed to protect subprime borrowers.

HPMLs are subject to specified restrictions. Creditors of HPMLs must assess the consumer's ability to repay the loans, the loans are subject to restrictions on prepayment penalties, and the loans require escrow accounts in many instances.

The DFA similarly requires that creditors verify consumers' ability to repay,[53] restricts prepayment penalties,[54] and mandates escrow accounts for many loans.[55] New rulemakings in these areas are imminent, which are very likely to replace § 226.35. There appears no purpose to revising the now-obsolete § 226.35 apart from the related DFA rulemakings.

The DFA also introduces APR-to-APOR comparisons for HMDA reporting,[56] ability-to-repay determinations,[57] *bona fide* discount point definition,[58] prepayment penalty restrictions,[59] HOEPA loan rate threshold,[60] appraisal requirements for higher-risk mortgages,[61] and mandatory escrow requirements.[62] We would support incorporating the TCR into these comparisons.

If the Board were to pursue its proposal to require a chart comparing the disclosed APR with the APR for loans in the "high cost zone," the chart should not be misleading. If the

[53] TILA § 129C(a), added by DFA § 1411(a)(2), 24 Stat 1376, 2142-45 (2010).
[54] TILA § 129C(c), added by DFA § 1414, 24 Stat 1376, 2149-50 (2010).
[55] TILA § 129D, added by DFA § 1461, 24 Stat 1376, 2178-81 (2010).
[56] Home Mortgage Disclosure Act § 304(b)(5), as amended by DFA § 1094(3)(iv), 24 Stat 1376, 2097 (2010).
[57] TILA § 129C(a)(6)(D)(ii), added by DFA § 1411, 24 Stat 1376, 2144 (2010).
[58] TILA § 103(dd)(1) and (2), added by DFA § 1431, 24 Stat 1376, 2160 (2010).
[59] TILA § 129C(c)(1)(B)(ii), added by DFA § 1414, 24 Stat 1376, 2149-50 (2010).
[60] TILA § 103(aa)(1)(A)(i), as amended by DFA § 1431, 24 Stat 1376, 2157 (2010).
[61] TILA § 129H(f)(2), added by DFA § 1471, 24 Stat 1376, 2187 (2010).
[62] TILA § 129D(b)(3), added by DFA § 1461, 24 Stat 1376, 2178-79 (2010).

chart were to use the disclosed APR, it would inadvertently tell consumers that the loan is a high-cost loan when it is not, or that it is closer to a high-cost loan than it actually is. This would be inappropriate.

A preferable solution to this problem would be to revise the APOR calculation to make the comparisons with the APR more accurate. The APOR currently includes some, but not all, prepaid finance charges. Including in the APOR everything required to be included in the prepaid finance charge would make for the best disclosures because it would make the comparison most meaningful.

Some of the charges vary geographically, but this is mainly due to government charges, which are known. We suggest three separate APOR calculations for high, medium, and low cost counties.

Revising the APOR would have several significant benefits. Most importantly, it would make the comparisons to the APR more accurate because the comparison would look at the same cost items. Including some costs in the APR but not in the APOR would mislead consumers. It would also defeat the purpose of making the comparison in the first place.

Using the same APOR calculation for all the new APR-to-APOR comparisons would greatly ease compliance burdens. It would also make HMDA data easier to understand.

Further, some states use the Regulation Z comparison of the APR to the APOR for defining whether a loan is a high cost loan under state law. For this reason, including costs in the APR but not in the APOR would inadvertently cause some prime loans to be treated as restricted subprime loans.

Points and Fees Definition

We strongly support the Board's proposal to preserve the current treatment of third-party charges under the HOEPA points and fees test. This is important because it would prevent prime loans from meeting the HOEPA threshold and similar thresholds under state law.

We note that the DFA amends the definition of points and fees in TILA section 103. We believe the reasoning behind the proposed exclusion from the points and fees calculation should carry forward under the DFA definition. We urge the Board to coordinate the proposed definition with the new DFA definition. The definitions should be made together in one rulemaking so that they will be coordinated.

FHA Prepayment Penalties

The DFA also makes obsolete one aspect of the present rulemaking affecting prepayment penalties on FHA loans.

FHA loans use a monthly interest accrual amortization method, under which payments are treated as made on the scheduled payment due date even if they occur on a different date. Under this method, if a consumer pays off an FHA loan after a scheduled payment due date and during the grace period for that due date, the consumer owes interest only until the scheduled payment due date. The consumer is charged no interest for a period of time while the loan is outstanding. If payoff occurs after the grace period but before the next scheduled payment date, the consumer owes interest through the following scheduled payment date. That is, the consumer owes interest for a few days although the loan is paid off. The Board proposes to treat any interest paid after loan payoff as a prepayment penalty.

We do not object to requiring disclosure of the FHA accounting method. However, we recommend coordinating the FHA prepayment penalty treatment with the DFA.

Under the Board's proposal, disclosures for FHA loans would need to alert consumers to the possibility of a prepayment penalty even if the creditor does not intend to charge the consumer for interest after payoff. HPML loans may not have a prepayment penalty more than two years after consummation. By treating the FHA accounting method as a prepayment penalty, the proposal would prohibit FHA loans from being HPML loans. That will have a significant unintended impact on FHA credit availability.

The DFA bans prepayment penalties on loans that are not a "qualified mortgage," a term that does not yet have a definition.[63] If an FHA loan were to have a prepayment penalty, if would need to be a qualified mortgage. Importantly, Congress directed FHA, not the Board, to define qualified mortgage for FHA purposes.[64] Defining qualified mortgage necessarily involves setting prepayment penalty restrictions because only qualified mortgages may have prepayment penalties. Were the Board to finalize its proposal, it would interfere with the FHA's authority to determine the appropriate prepayment penalty restrictions on FHA loans.

The DFA also created a "qualified residential mortgage." This term is not yet defined, but must be "no broader" than the definition of qualified mortgage.[65] Congress again specifically exempted FHA from the restrictions relating to qualified residential mortgages,[66] so that FHA, not the Board, will determine the appropriate prepayment penalty rules for FHA loans.

For these reasons, we do not believe there is any longer a reason for the Board to revise the Regulation Z prepayment penalty treatment of the FHA's monthly interest accrual amortization method.

Credit Protection Products

The Board proposes revised disclosures concerning credit protection products. We note that these products are highly regulated by the states. Credit protection products can be benefit to consumers by permitting them to retain their homes despite death, illness, or

[63] TILA § 129C(c)(1)(A), added by DFA § 1414, 24 Stat 1376, 2149 (2010).
[64] TILA § 129C(b)(3)(B)(ii)(I), added by DFA § 1412, 24 Stat 1376, 2148 (2010).
[65] DFA § 941, 124 Stat. 1376, 1895 (2010), to be codified at 15 U.S.C. § 78o-11(e)(4)(C).
[66] DFA § 941, 124 Stat 1376, 1894 (2010), to be codified at 15 U.S.C. § 78o-11(e)(3)(B).

loss of income by the family member whose income covers the mortgage loan payments. Many consumers lack sufficient life insurance to cover their mortgage credit. We believe it would be inappropriate for disclosures to lead consumers to believe that the products are harmful when they can be beneficial.

We also note that the DFA rulemakings may affect the treatment of credit protection products, such as by including their cost in new debt-to-income definitions.[67] We recommend that the Board amend the rules for credit protection only in a rulemaking that is coordinated with the DFA rulemakings.

Revocable Living Trusts

We appreciate the Board's proposal to clarify the applicability of Regulation Z to revocable living trusts. We request further clarification. It is not clear whether disclosures should be provided to the settlor, the trustee, or to the beneficiary. It is also not clear which of the parties would have the right to rescind the loan.

In the case of a rescission under an extended right to cancel, the trust would be obligated to return principal under TILA § 125. However, the trust terms may be not permit this. We recommend clarification that rescission in the case of a trust not be available if return of principal is restricted by the trust arrangement.

Alternative Approaches for Corrected Disclosures

The Board proposes two alternatives for requiring corrected disclosures and a new waiting period if an early disclosure becomes inaccurate. We urge the Board to consider this question in connection with the RESPA requirements. RESPA rules often require a number of revised disclosures, far too many on some loans. Deluging a consumer with multiple disclosures is not helpful.

We support revising disclosures only when it would be helpful to consumers. For this reason, we prefer the alternative of requiring a corrected disclosure only when an APR included in an early disclosure becomes inaccurate, or when a risky feature is added to a loan.

The proposal would not require a corrected disclosure when the APR decreases by more than the tolerance only if the decrease was due to a discount for making payments by automated debits or for a discount on voluntary owner's title insurance. These exceptions are far too narrow.

An APR should be considered accurate whenever an inaccuracy is due to an overstated finance charge because overstatements do not harm consumers as understatements do. A corrected disclosure should not be required when the rate is decreased and the APR is overstated because the disclosed finance charge and APR reflect overstated interest charges in the scheduled payments.

[67] TILA § 129C(b)(2)(A)(vi), added by DFA § 1414, 24 Stat 1376, 2146 (2010).

A corrected disclosure should not be required when a closing cost included in the finance charge is lower than the amount estimated in the previous disclosure.

Closing agents, not creditors, control the amounts actually paid at closing. For this reason, limits on using estimating fees in disclosures are inappropriate unless the Board also requires closing agents to provide the creditor with the final amounts of all fees before consummation.

Irregular Transactions

It is not clear whether the proposal would affect current Comment 17(c)(1)-10(iv). This comment states that ARMs whose initial rates are not calculated using the index or formula used for later rate adjustments are irregular transactions. The proposal does not seem to amend this comment. Proposed § 226.22(a)(3) defines irregular transactions, but does not include those ARM loans. We are not sure whether the Board proposes to delete this Comment.

HMDA

The Board seeks comment on whether "refinancing" under Regulation C should include a "new transaction" under proposed § 226.20(a)(1). In part, this will depend on which transactions the new rule will cover.

The Home Mortgage Disclosure Act (HMDA) describes its purpose:

> The purpose of this title is to provide the citizens and public officials of the United States with sufficient information to enable them to determine whether depository institutions are filling their obligations to serve the housing needs of the communities and neighborhoods in which they are located and to assist public officials in their determination of the distribution of public sector investments in a manner designed to improve the private investment environment.[68]

If the Board were to apply this rule to transactions that bear directly on housing needs, then HMDA reporting may be appropriate. But if the new rule were to apply to minor transactions that do not have much bearing on housing, reporting those minor transactions may introduce "noise" into the HMDA data and devalue its usefulness.

We note that the DFA added new HMDA reporting requirements, and that there may soon be a new HMDA rulemaking to implement these changes.[69] We suggest that it would be preferable to consider all HMDA issues together, in that rulemaking rather than in the present rulemaking.

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[68] Home Mortgage Disclosure Act § 302(b), 12 U.S.C. § 2801(b).
[69] DFA § 1094, 124 Stat 1376, 2097-2101 (2010).

SAFE Act

The Board solicits comment on whether there would be operational difficulties in defining "loan originator" for SAFE Act purposes to exclude those who work on modifications of existing loans, although those modifications may be modifications. The operational problem would be subjecting modifications to Regulation Z and TILA. Modifications are straightforward transactions about which consumers can make a decision quickly because little changes. The operational burden of providing TILA disclosures would be disproportional to the substance of modifications.

Regulatory Burden

The Board estimates:

> The proposed rule would impose a one-time increase in the total annual burden under Regulation Z for all [1138] respondents regulated by the Federal Reserve by 190,168 hours, from 1,497,362 to 1,687,530 hours. In addition, the Board estimates that, on a continuing basis, the proposed revisions to the rules would increase the total annual burden by 610,464 hours from 1,497,362 to 2,107,826 hours.[70]

It then estimates that respondents would need 160 hours to implement proposed §§ 226.15 and 226.23, 8 hours to implement advertising requirements of proposed § 229.16, and 160 hours to implement proposed § 226.33.[71]

As just one example, one large lender expended over 70,000 hours to implement the Regulation Z amendments that became effective October 1, 2009, while implementing the recent amendments to Regulation X took twice that amount of time.

In its Initial Regulatory Flexibility Analysis, the Board states:

> The Board has not identified any Federal rules that conflict with the proposed revisions to Regulation Z.[72]

We have described in this letter a significant conflict the proposal would have with RESPA rules. Further, this proposed rule does not integrate RESPA and TILA disclosures. The proposal therefore conflicts with the integration that the DFA mandates.

We urge the Board to address these conflicts before pursuing this proposal. It would be counterproductive for the industry to come into compliance with this very major proposed rule, which will soon be replaced by new DFA rules.

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[70] 75 Fed. Reg. 58539, 58684 (September 24, 2010).
[71] 75 Fed. Reg. 58539, 58684-85 (September 24, 2010).
[72] 75 Fed. Reg. 58539, 58687 (September 24, 2010).

The Regulatory Flexibility Act requires the Board's Initial Regulatory Flexibility Analysis to contain:

> [A] description of any significant alternatives to the proposed rule which accomplish the stated objectives of applicable statutes and which minimize any significant economic impact of the proposed rule on small entities.[73]

There is one alternative that would minimize the economic impact of the proposal on small entities and on consumers. That would be to pursue changes to Regulation Z only with RESPA integration and with other related DFA rules.

In this letter, we suggest alternatives to the proposal to include third party charges in determining rescission tolerances. Our recommendations would reduce the economic impact on small entities and on consumers,

We note that we had difficulty following precisely what regulatory text is proposed in this rulemaking. The Board refers to its 2009 proposals in some places in the preamble to the present proposal, but does not include all of the regulatory text of the prior proposals in the regulatory text of this proposal. The Board republished in this proposal some portions of prior proposals, such as in § 226.20(c), but does not consistently republish other parts of its prior proposals that are still effective. We are unsure what meaning to read into this inconsistent treatment. We suggest that the Board could reduce regulatory burden by including all proposed changes in one *Federal Register* publication, or on its website, if that would be more practical.

Conclusion

We appreciate the Board's efforts to improve TILA disclosures for consumers.

As noted at the beginning of this letter, we urge the Board not to amend Regulation Z until its amendment can be integrated with RESPA and with the many changes that the DFA rulemakings will introduce. The best approach would be to make the amendments together at one time. This would prevent inadvertently making changes that conflict. It would also prevent making changes now, only to have to revise them again once the DFA is implemented.

Sincerely,

Anne C. Canfield
Executive Director

[73] Regulatory Flexibility Act § 603(c), codified at 5 U.S.C. § 603(c).