PrimeLending
A PlainsCapital Company

July 22, 2011

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

Re: 12 CFR Part 226
Regulation Z
Docket No. R-1417
RIN 7100-AD75

Dear Secretary Johnson:

I appreciate the opportunity to submit this letter of comment on the proposed rule to implement ability-to-repay requirements and establish qualified mortgage provisions for closed-end residential loans (the "Proposed Rule") as mandated by Sections 1411, 1412 and portions of 1414 of the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act of 2010 ("Dodd-Frank" or "the Act") on behalf of PrimeLending, a PlainsCapital Company ("PrimeLending").

History and Business of PrimeLending and PlainsCapital Bank

PrimeLending was established in 1986 by Ms. Roseanna McGill, and since 2000 it has been a wholly-owned subsidiary of PlainsCapital Bank, one of the largest independent banks in the United States and a member of the Federal Reserve System, the deposits of which are insured by the FDIC. PrimeLending lends in all 50 states and the District of Columbia, and we have more than 1,900 employees and offices in 38 states. PrimeLending is a retail mortgage loan originator that funds and closes loans in its own name using a warehouse line of credit. With rare exceptions, the loans originated by PrimeLending are sold on the secondary market to various investors.

According to MortgageDataWeb.com, PrimeLending is currently the 13th largest retail loan originator in the United States, with approximately $7.6 Billion in mortgage loan originations in 2010. PrimeLending was ranked as the number three Federal Housing Administration (FHA) lender in Texas and the number 13 FHA lender in the United States for 2010.

We believe our greatest success is the profound positive impact of our business on American families. In 2010, PrimeLending funded approximately $4.5 billion in purchase money loans, which helped almost 25,000 families achieve the dream of homeownership. PrimeLending also made over $2.5 billion in refinance loans and $715 million in cash-out refinance transactions, helping reduce the debt burden for about 11,000 families/individuals (refinance) and providing cash for such projects as home improvement, education, or debt consolidation for over 3,500 families/individuals (cash-out refinance).

As a retail mortgage loan originator, PrimeLending accepts loan applications from individuals interested in a mortgage loan, and then processes, underwrites, closes and funds loans from a warehouse line of credit provided by PlainsCapital Bank. PrimeLending employs a first-rate staff of dedicated underwriters who ensure that each loan meets the stringent requirements imposed by state and federal regulations, as well as the high expectations of our secondary market investors. After a loan is closed and funded, PrimeLending sells individual whole loans to investors in the secondary market. Typically, PrimeLending will identify an investor that will purchase each loan when it is originated, and we underwrite each loan according to that investor's guidelines, in order to ensure that each loan can be sold into the secondary market as efficiently as possible.

The Dodd-Frank Act

Section 1411 of the Dodd-Frank Act amends the Truth in Lending Act by requiring that mortgage lenders determine a borrower's ability to repay a mortgage loan. The Act sets forth the criteria for establishing ability to repay in Section 1411. If the loan satisfies the definition of a "qualified mortgage" (QM) set forth in Section 1412 of the Act, the lender is deemed to have satisfied the ability to repay standard established by Section 1411, and is entitled to certain legal protections in connection therewith.

Section 1412 provides that a QM is a residential mortgage loan:

- In which total points and fees do not exceed 3 percent (3%) of the total loan amount;
- That does not provide for negative amortization or deferral of principal payments;
- That does not provide for a balloon payment that is more than twice as large as the average of earlier scheduled payments;
- In which the borrower's income and financial resources have been verified;
- Where loan has a fixed interest rate, the underwriting process is premised upon a repayment schedule fully amortizing the loan over the loan's term taking into account all applicable taxes, insurance and homeowner association assessments; and
- Where the loan has an adjustable interest rate, the underwriting process is premised upon the maximum permissible rate during the first five years, and a payment schedule that fully amortizes the loan over the loan's term taking into account all applicable taxes, insurance and homeowner association assessments.

Since Section 1413 of the Act provides that a borrower may, among other things, assert a violation of Section 1411 as a defense to any foreclosure or debt collection action, it is essential that the legal protections of Section 1412 are effective. Please allow us to articulate our concerns with, and recommendations regarding, Section 1412 and the Proposed Rule.

The Proposed Rule

Pursuant to the requirements of the Act, the Board of Governors of the Federal Reserve System (the "Fed") issued an extensive (474 page) Proposed Rule implementing the requirements of the Act with respect to the Fed's Regulation Z (12 CFR Part 226). Although not readily susceptible to a short, accurate summary, the proposal provides, as required by the Act, that a lender is prohibited from making a mortgage loan unless it is determined, utilizing verified and documented information, that the borrower will have a reasonable ability to repay the loan, including any mortgage-related obligations (such as property taxes and insurance). The Proposed Rule further mandates that the lender must consider several factors in making the ability-to-repay determination, including the borrower's income and assets, employment status, proposed monthly payment on the loan, payments for obligations related to the loan (such as ad valorem taxes and homeowner's insurance), other debt obligations, debt-to-income ratios, and credit history.

Under the Act and the Proposed Rule, lenders may choose to originate QM loans providing protections for lenders from liability for accusations concerning a violation of the lender's obligation to determine a borrower's ability to repay. The Fed notes that the Act is somewhat unclear concerning details of the protections to be afforded lenders, and it proposed two alternative approaches for such protections. The Fed requests comments on which alternative to utilize. The first alternative would provide a legal safe harbor and define a QM as a mortgage loan:

- For which total points and fees do not exceed three percent (3%) of the total loan amount;
- That does not contain negative amortization, interest-only payments, a balloon payment, or a loan term exceeding 30 years;
- For which income or assets relied upon in making the ability-to-repay determination are considered and verified; and
- Where underwriting of the loan (i) is based on the maximum interest rate that may apply in the first five years, (ii) utilizes a payment schedule fully amortizing the loan over the loan term, and (iii) takes into account any mortgage-related obligations.

A second alternative QM formulation proposed by the Fed would provide a rebuttable presumption of compliance and would define a QM as including the criteria provided for in the first alternative, above, as well as additional underwriting requirements, including consideration and verification by the lender of:

- The consumer's employment status;
- The monthly payment for any simultaneous mortgage;
- The consumer's current debt obligations; and
- The consumer's monthly debt-to-income ratio.

<u>Safe Harbor</u>

PrimeLending supports and recommends adoption of the first alternative, or safe harbor approach, for compliance with only minor changes. The certainty provided by the safe harbor is absolutely critical to the smooth operation of the mortgage lending industry. Without the certainty provided by a safe harbor, the ability of the industry to efficiently service loans would be significantly impaired. Although PrimeLending is not a loan servicer, it makes extensive representations and warranties about the loans that it sells to its investors. PrimeLending is also subject to extensive indemnification and loan repurchase obligations in its agreements with its investors. In the event a borrower alleges that their ability to repay was not correctly determined pursuant applicable legal requirements, the investor that bought the loan will, if permitted pursuant to their agreements with PrimeLending, seek remedies from PrimeLending to the extent that they suffer a loss. The nature of the mortgage lending business today is such that the implications of this issue cannot be overstated: virtually any defaulting borrower will be tempted to assert an action in response to a lender's foreclosure in the hope that some lender violation of the ability to repay requirement can be established in the litigation. The potential for this liability and the costs associated with defending such suits mandate the need for a clear safe harbor that can quickly and efficiently resolve disputes where there has been no violation of the lender's determination of the borrower's repayment ability. Accordingly, bright-line certainty with respect to a lender's satisfaction of its obligation to determine the ability to repay is absolutely critical for PrimeLending and the mortgage lending industry.

The second alterative proposed by the Fed, the mere rebuttable presumption, is insufficient and would provide only the illusion of material protections for lenders. Generally, a rebuttable presumption is nothing more than a fact taken to be true by a tribunal until a party disputes it and provides some evidence, which might consist of a borrower's testimony, contradicting the presumption. In other words, the presumption is valid only for so long as it is uncontested by the borrower. The inherent deficiency of this approach from PrimeLending's perspective is that a rebuttable presumption serves as no real protection for a lender—such a presumption offers little legal protection that the lender does not already have. PrimeLending understands that Congress intended that there be "special protections" afforded QM loans and the lenders making and servicing them. In short, more than a mere rebuttable presumption must be provided to mortgage lenders to ensure real legal protections for lenders and mortgage loan investors and to mitigate the potentially material costs of frivolous litigation instigated to delay and create negotiating leverage.

<u>Recommended Adjustments to the Criteria for QMs – Points and Fees</u>

The limitation of points and fees to three percent (3%) is unreasonably low, especially when dealing with low (small) loan amounts. PrimeLending recommends that the Fed utilize its authority under the Act to adopt the approach that PrimeLending and many in the industry have used successfully for several years: the five percent (5%) limitation promulgated by Fannie Mae. One approach would be to eliminate the small loan threshold altogether with lenders permitted to charge up to five percent for all loans. Alternatively, the small loan threshold proposed by the rule as $75,000 should be increased to $150,000 and the tight tiers proposed for small loans should be eliminated with lenders permitted to utilize up to five percent (5%) of loan amount. In this way, the rule's effect on the availability of credit for low and moderate income borrowers will be minimized because many of a lender's costs for making small loans substantially similar as for larger loans and the limitations proposed by the Fed will make it extremely difficult, if not impossible, for lenders to profitably make smaller loans. This five percent (5%) approach has been an industry standard since first promulgated by Fannie Mae several years ago, and it has proven a workable standard for mortgage loan originations in PrimeLending's experience.

The rule should also explicitly clarify that fees which are not paid to a lender or lender affiliate should not be included in the three percent (3%) limitation. Charges imposed by third parties, such as settlement agents and title insurers unaffiliated with the lender should not be included in the three percent (3%) limitation. Including these charges will make it extremely difficult for lenders to cover their origination costs, especially for smaller loan amounts. Similarly, compensation paid by the lender to the loan originator, whether a lender employee or third-party (affiliated or unaffiliated), should not be included in the three percent (3%) calculation. Loan originator compensation has been extensively addressed by the Fed's previous Reg Z rulemakings, and further regulation of this matter thorough the QM definition is unwarranted.

Conclusion

As can be discerned from the foregoing, we at PrimeLending have deep reservations about both the use of a rebuttable presumption of compliance with QM requirements and certain aspects of the definition of QM contained in the Proposed Rule. Adopting the rebuttable presumption approach and the QM definition as proposed will have an adverse impact on the ability of mortgage lenders to continue to provide competitively priced and readily available loan funds to borrowers and, in turn, provide a vital stimulus to the economy and the financial wellbeing of our borrowers.

We urge the Fed to reexamine the Proposed Rule and to amend the proposal to mitigate the concerns and effects expressed in this letter. PrimeLending recommends and requests that the Fed utilize its authority pursuant to Section 1412 of the Act to amend the definition of "Qualified Mortgage" in the Proposed Rule to account for the foregoing issues. Making the recommended changes will facilitate a robust mortgage lending market with the concomitant required consumer protections. Moreover, making the proposed revisions will ensure that the mortgage needs of American families—including low and moderate income families—will continue to be met.

Sincerely,

Todd Salmans,
President and CEO
PrimeLending, a PlainsCapital Company