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July 22, 2011

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

RE: Docket No. R-1417; RIN No. 7100-AD75

Dear Ms. Johnson:

On behalf of the undersigned civil rights organizations, we submit the following comments on the Board's proposed rule amending Regulation Z (Truth in Lending) to implement amendments made to the Truth in Lending Act by the Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted one year ago.

Our organizations commend the Board for its detailed assessment of the issues addressed in the statute and the thoroughness of its proposed rule. This section of the statute was intended to reset the approach of the mortgage lending industry, which had strayed too far from the application of sound underwriting standards for mortgage loans. The industry targeted families and communities of color and many other protected classes for unsustainable, risky subprime loans without regard to the ability to repay and relied on false presumptions of market behavior.

This proposed rule's reorientation to sensible underwriting cannot come a moment too soon. We are all suffering the painful consequences of the risky mortgage lending practices of recent years, as foreclosures have spiraled and home values have plummeted. Household wealth nationwide has dropped by $6 trillion since 2006.[1]

Communities of color have been devastated by these risky lending practices. Those communities were targeted for loans that were unsustainable and often predatory, and, as a result, homeowners of color face foreclosure at substantially higher rates than their white counterparts.[2]

The homeownership gaps between whites and people of color have gotten worse or remained stagnant, in spite of much rhetoric in recent years describing the increase in minority homeownership. These increases have been outpaced or matched by increases in white homeownership. For example, **the homeownership gap between whites and African-Americans has gotten worse.** The gap in 1940 was 22.8 percentage points, in 1960 was 26.2 points, in 1995 was 28, and in 2010 was 28.5 percentage points.[3] **The homeownership gap between whites and Hispanics has improved by only two percentage points** from 28.9 in 1995 to 26.9 in 2010.[4]

Even those who have been able to hold onto to their homes have suffered financial losses. The amount of wealth drained from African-American and Latino communities due to the depreciation in values of property located near foreclosures has been estimated at $194 billion and $177 billion, respectively, for a combined total of over $371 billion.[5] These losses will have substantial, negative, long-term impacts on the financial security and well-being of families of color in the United States. Families of color will soon constitute the majority of our country's population; thus, these negative impacts affect us all.

We need to rebuild the road to sustainable homeownership, and to do so, we must put mortgage lending practices back on solid footing, re-aligning the interests of borrower, lender, securitizer and investor. A number of provisions in the Dodd-Frank Act address this balance; none is more important than the "ability to repay" standards. We cannot overstate the importance we place on strong rules regarding lenders' responsibility to make mortgages based on a realistic assessment of the borrower's

[1] Center for Responsible Lending Research Brief, "Big Bank Payday Loans," July 21, 2011.
[2] Center for Responsible Lending Research Report, "Foreclosures by Race and Ethnicity: The Demographics of a Crisis," June 18, 2010
[3] Leigh, Wilhemina and Huff, Danielle, "African Americans and Homeownership: Separate and Unequal, 1940 to 2006." Joint Center for Political and Economic Studies, Brief #1, November 2007 p.4; and "State of the Nation's Housing 2011," Joint Center for Housing Studies of Harvard University, p. 36.
[4] Ibid Joint Center for Housing Studies of Harvard University.
[5] Ibid Center For Responsible Lending Research Report.

ability to repay the loan. The Board has taken a critical first step in this proposed rule, and we expect that the Consumer Financial Protection Bureau will finish the job effectively.

Safe Harbor vs. Rebuttable Presumption

A central question in the Board's proposed rule is whether Congress intended that lenders that originate a "qualified mortgage" would have a "safe harbor" from liability or whether the standards are intended to create a presumption of compliance which the borrower has the opportunity to rebut in defending against foreclosure or other collection action. We strongly urge adoption of the second approach.

Rebuttable presumption is the approach clearly contemplated by the statute which, in Sec. 1413 Defense to Foreclosure, states the following:

> "Notwithstanding any other provision of law, when a creditor, assignee, or other holder of a residential mortgage loan or anyone acting on behalf of such creditor, assignee, or holder, initiates a judicial or non-judicial foreclosure of the residential mortgage loan, or any other action to collect the debt in connection with such loan, a consumer may assert a violation by a creditor of paragraph (1) or (2) of section 129B(c), or of section 129C(a) as a matter of defense by recoupment or set off without regard for the time limit on a private action for damages under subsection (e)."

The creation of a safe harbor is entirely inconsistent with this newly created defense to foreclosure or other collection action. In addition, neither the statutory language nor the legislative history of Dodd-Frank indicates that Congress intended to create a safe harbor. The *only* reference to "safe harbor" appears in the *caption* to section 1412 of Dodd-Frank, which reads "Safe Harbor and Rebuttable Presumption." But for this inadvertent caption, there would be no ambiguity.

<u>The Section 1412 caption is merely a left-over caption of an earlier version of the proposed Mortgage Reform and Anti-Predatory Lending Act which created a dual track for liability: a rebuttable presumption for creditors and a safe harbor for certain secondary market parties</u>. Subtitle B of Dodd-Frank's Title XIV, containing both the ability to repay provision (Section 1411) and the qualified mortgage provision (Section 1412) evolved from these earlier versions of the so-called "Miller-Watt-Frank" anti-predatory lending proposals.

Further, ongoing robo-signing scandals continue to demonstrate that the lending industry is capable of massive, widespread errors in originating and securitizing mortgages, and that the federal regulatory apparatus is not always capable of detecting – let alone preventing – such abuses. Even when industry missteps are uncovered, the federal government lacks the resources to review each loan originated by a number of large lenders over a multi-year period. While we hope that the Consumer Financial Protection Bureau will oversee mortgage origination and servicing more aggressively than federal regulators have in the past, Congress intended that the individual borrower should be able to rebut the presumption that the lender fully considered borrower's ability to repay the mortgage obligation.

Finally, we are puzzled by the more limited standards the Board has proposed for the "safe harbor" alternative. The proposed standard for a safe harbor contains some of the same elements as those for the proposed rebuttable presumption, but does not include consideration or verification of the borrower's employment status, monthly payment for any simultaneous mortgage, current debt obligations, debt-to-income ratio or residual income, or credit history. If a standard were to be adopted that provided creditors with blanket protection from liability, <u>an alternative we oppose,</u> such a standard should be more – rather than less – rigorous than the standard offered for the rebuttable presumption of compliance, under which borrowers may have the opportunity to show that the creditor has violated the ability to repay requirements of the regulation. Where there is less judicial scrutiny of the transaction, as would be the case with the safe harbor, the standard for avoiding liability should be higher, not lower.

In addition to the safe harbor/rebuttable presumption questions, we have the following comments on other aspects of the proposed regulation.

General Ability to Repay Requirement

We support the elements the Board has proposed to determine a borrower's ability to repay a mortgage loan, including verified income and assets, monthly payment on the covered transaction and any loan made simultaneously, current debt obligations, debt-to-income ratio or residual income, and credit history. Had such standards previously been in place, the foreclosure crisis and economic disruption we are currently facing would have been avoided. In addition, we support the use of the greater of the introductory interest rate or the fully-indexed interest rate, as defined in the proposed regulation, as the basis for deriving the amount of the mortgage payment that will be used for the ability to repay calculation. In addition the fully-indexed rate may underestimate payment increases at reset and therefore ARMs outside of the qualified mortgage should be underwritten to several points above the fully-indexed rate.

We urge the Bureau to be clear that, in verifying income, creditors should not establish different standards for different types of income. In particular, **we are concerned that some creditors take different steps to verify the income of borrowers who are employed and those who receive disability income**. For the former, creditors may simply seek verification of income by using a tax return transcript issued by the IRS or payroll statements, among other methods listed in the proposed rule.

For borrowers receiving disability income, we understand that some creditors require a letter stating that the income is guaranteed for three years, or some other specific period of time, into the future. Such a letter is virtually impossible for borrowers to obtain. The Social Security Administration, a primary source of disability income, does not provide such letters, although it will provide verification that the borrower currently receives disability income. Employed borrowers generally cannot prove that they will continue to be employed for a specific period of time, and there is no reason to permit creditors to hold borrowers who receive disability income to a different standard. Such a double standard is a violation of the federal Fair Housing Act, which prohibits discrimination on the basis of disability in the terms and conditions of housing transactions, including financing for a home purchase or refinance transaction. We urge the Bureau to include such a prohibition in its final rule or, at a minimum, include in its Commentary that imposing different requirements for verification of income for disabled loan applicants violates fair lending laws.

In addition, we want to raise a caution about the use of credit history, as reflected in the credit reports and credit scores provided by the major credit bureaus. While credit records may be useful for documenting the types and amounts of a borrower's credit obligations, they also have their limitations, particularly for determining a borrower's willingness to repay a mortgage. For example, when borrowers make use of non-traditional sources of credit, those transactions may not be reported to the credit bureaus. In those cases, the creditor may need to look elsewhere in order to obtain a complete overview of the borrower's credit history. Further, a great many borrowers in recent years were targeted for unsustainable mortgages, including hybrid subprime adjustable rate mortgages (ARMs), payment option ARMS, and interest only loans. Borrowers of color were disproportionately targeted for such loans. The fact that many were unable to afford the payments on their loans over time was a function of the fatally flawed design of the loan product, not the borrowers' willingness to repay the loans. It is crucial not to establish a set of lending standards that perpetuates the discriminatory practices of the past by basing future access to mortgage credit on an unfair and inaccurate standard. The final rule should include the requirement that the lender consider a borrower's explanation of the type of loan product and circumstances that resulted in the negative credit history.

Qualified Mortgages

We strongly support adoption of Alternative 2 for the definition of a qualified mortgage as a fully amortizing loan with regular periodic payments, no negative amortization or balloon payments, a maximum term of 30 years, with points and fees limited to 3% of the total loan amount, underwritten using all mortgage-related obligations and the fully indexed interest rate, and where the creditor has considered and verified the consumer's employment status, monthly payment for any simultaneous mortgage, current debt obligations, debt-to income ratio or residual income, and credit history. While we have some cautions about how creditors consider some of these factors, as described above, we believe that this is a comprehensive list of the factors that should properly be required for the underwriting decision if the creditor is entitled to a presumption of having considered ability to repay in the event of the borrower's default.

We recommend including the additional requirement that when assessing the consumer's income and determining whether the consumer will be able to meet the monthly mortgage payments, that other recurring but non-debt related expenses also be taken into account. Many consumers, and especially low- and moderate income consumers, face significant monthly recurring expenses. While these will not show up as debt or mortgage related expense, they nevertheless can make a large claim on disposable income and, together with a mortgage payment, consume an unreasonably large portion of a household's income. Such expenses as medical supplies or prescriptions and child care expenses needed to enable the borrower or co-borrower to work outside the home are only two important examples of such obligations. We strongly believe that the qualified mortgage standard should require lenders to consider such obligations in making the overall determination of whether a consumer has the ability to repay the proposed mortgage debt.

We also support the option proposed for a creditor to originate a mortgage that receives qualified mortgage designation when the creditor is refinancing a non-standard mortgage with risky features into a more sustainable standard mortgage. This option will provide much-needed relief for borrowers whose loans are not sustainable over the long run, but who are not yet in default. Given the patterns of mortgage lending in recent years, whereby borrowers of color have been targeted for unsustainable loans, we believe that this option will help prevent further foreclosures and loss of wealth in communities of color, as well as for homeowners in general.

Limits on Points and Fees

The proposed rule sets a general limit on points and fees of 3% of the total loan amount. We support this limit, which will prevent the kind of abusive pricing that has characterized some parts of the mortgage market, most particularly in communities of color. At the same time, this limit will provide a reasonable balance between the interests of the borrower and the lender.

Exception to Limits on Points and Fees for Small Transactions

We support the Alternative 2 mathematical formula because it is more beneficial to the borrower.

The proposed rule allows creditors to exceed the 3% limit on points and fees for loans with a principal balance of $75,000 or less, and proposes two alternative approaches for determining the maximum points and fees that could be charged for smaller loans. The Board bases this exception on the understanding that creditors face fixed costs to originate mortgage loans, and that 3% of a small loan may not be enough to cover those fixed costs. If that were the case, the 3% cap would disadvantage lenders who tend to make predominantly small loans – small institutions and those operating in lower income and rural areas. Those lenders would not be able to make up the shortfall with fees from larger loans.

We appreciate this concern, and support the Board's effort to make sure that the rule does not create undue barriers to access to credit in low and moderate income communities or other areas where housing prices tend to be lower. At the same time, however, we caution that this goal must be balanced against the interests of individual borrower seeking small loans. While offering some flexibility in pricing may be a good thing, we must avoid setting up certain groups of borrowers for disparate pricing schemes, under which they are charged an unfair premium for small balance loans. Many of these borrowers are likely to be low and moderate income people and/or people of color, since housing prices in these communities are historically lower. To prevent unfair pricing for small loans, it is important to make sure that the premiums charged are kept within reasonable bounds, and reflect the actual costs of loan origination.

Single Premium Credit Insurance

We applaud the restrictions on the sale of single premium credit insurance contained in the proposed rule. Single premium credit insurance, where the entire premium is paid up front and generally rolled into the principal balance of the loan, is a product that is very lucrative for lenders, but all too frequently offers little, if any, value to the borrower. A great many borrowers have found, when they sought to collect under their policies, that they were not actually eligible for the benefits. Charging the premium up front in one lump sum makes it unaffordable for many borrowers, requiring them to roll it into the loan balance and pay it off, with interest, over 30 years. Not only do the interest charges increase the cost of the insurance, but because the term of the loan generally exceeds the term of the insurance, consumers are paying interest on the policy long after they can hope to receive any benefits under it. Given the limited benefits of this type of insurance, we applaud the restrictions on the sale of single premium credit insurance contained in the proposed rule. Furthermore a borrower could pay for this insurance on a monthly basis if he/she wanted to purchase this product rather than financing the entire premium at origination.

Limits on Pre-Payment Penalties

We applaud the limits on prepayment penalties proposed in this regulation, which should protect borrowers from this kind of trap in the future. A standard feature on subprime ARMs was a prepayment penalty that applied until, or in some cases beyond, the time at which the interest rate reset and the monthly payment increased. The widespread use of pre-payment penalties on subprime mortgages proved to be a mechanism that prevented borrowers from refinancing out of loans they could not sustain before those loans became unaffordable.

Mortgage-Related Obligations

We support the proposed rule's requirement for creditors to consider all of the borrower's mortgage-related obligations, not just the payment of principal and interest. One of the most troubling features of subprime loans was their lack of escrows for hazard insurance, taxes and any homeowner association dues. The failure to account for these costs enabled lenders to sell such loans to borrowers based on what appeared to be lower, affordable, monthly payments. Many borrowers with subprime loans lacking escrows defaulted on their mortgages when the unexpected property tax and homeowner's insurance bills were due. In many other instances, the servicer advanced the payments of property taxes and imposed high-cost lender-placed insurance when the borrower failed to pay the taxes and insurance. Consequently, the borrower's monthly payment increased significantly to repay the servicer for these advances, thereby resulting in an unaffordable new monthly payment and subsequent default. Requiring creditors to consider these costs will provide much-needed transparency to the mortgage lending process. Private mortgage insurance should also be included in a creditor's consideration of mortgage-related obligations. In addition, we urge adoption of the proposed requirement that the creditor must make the determination of ability to repay based on information verified from reasonably reliable records. All too often, unscrupulous loan originators provided unrealistically low figures for such mortgage related payments.

Thank you for considering our comments. This is an extremely important moment and opportunity to protect all borrowers, including borrowers of color and people with disabilities who have been targeted for unsustainable loans and required to meet unreasonable and discriminatory requirements. Please contact Debby Goldberg, National Fair Housing Alliance at 202-898-1661 or dgoldberg@nationalfairhousing.org with any questions.

Sincerely,

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