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April 29, 2011

*Via Electronic Submission*

Ms. Jennifer J. Johnson  
Secretary, Board of Governors  
Federal Reserve System  
20<sup>th</sup> Street and Constitution Ave.  
Washington, D.C. 20551

Re: Proposed regulations related to escrows (Docket No. R-1406 and RIN No. 7100-AD 65)

Dear Ms. Johnson:

AgStar Financial Services, ACA (“AgStar”) appreciates the opportunity to comment on the Federal Reserve’s proposed amendments to Regulation Z related to mandatory escrows for high-priced mortgage loans and related to additional disclosures regarding escrows that was published in the March 2, 2011 *Federal Register*.

AgStar, one of the nation’s largest Farm Credit associations, is a member-owned cooperative and a part of the Farm Credit System. One of AgStar’s primary missions, and indeed the primary mission of the entire Farm Credit System is to support agriculture and rural America. One of the ways associations like AgStar fulfill this mission is by offering home mortgage loans to farmers and residents of rural communities. AgStar is concerned that the proposed regulations fail to adequately consider the unique nature of home mortgage lending to farmers and other rural residents.

AgStar recognizes that amendments to the Truth in Lending Act were included in the Dodd Frank Wall Street Reform and Consumer Protection Act (“Dodd Frank Act”) passed by Congress in 2010, and appreciates the need for the Federal Reserve to promulgate regulations to implement those amendments. That said, it appears that the proposed regulations provide for a narrower exemption than required by the Dodd Frank Act. AgStar is concerned that an exemption that is too narrow will lead to fewer choices for consumers, especially consumers in rural communities, if smaller-volume lenders choose to not make home loans that would be subject to the new escrow requirements.

Home mortgage lending to farmers and rural residents creates unique challenges for lenders who are required to escrow funds for insurance and taxes. For example, many farmers have irregular or cyclical income that present unique cash flow challenges. Those challenges are significantly amplified by the new 5-year requirement contained in the Dodd Frank Act, which reduces

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flexibility that can be helpful to managing expenses in a way that is most consistent with the farmer's business operations.

Specifically, with regard to insurance, a farmer or rural homeowner often owns and insures buildings and structures in addition to the homestead. A typical farm policy will have significantly higher premiums and those premiums are subject to greater variability than a traditional homeowner's policy due in large part to frequent coverage changes necessary to manage the farming operation. This creates difficulty in performing accurate escrow analysis and can result in insufficient cushions and the need for the lender to remit premiums in excess of the funds collected from the homeowner. On the other hand, it can lead to a lender unintentionally collecting more than is necessary from the homeowner. Similar issues can arise related to taxes since home loans to farmers and rural residents often include larger acreages. Since the mortgaged property may include not just the homestead but farm land and other property, additional variability can exist that is unique to these types of home loans.

Because of the unique challenges associated with home mortgage lending to farmers and rural residents, AgStar urges the Federal Reserve to reconsider its proposed exemption from the escrow rules. The Dodd Frank Act expressly permits an exemption for lenders who operate "predominantly in rural or underserved areas" and do not exceed volume limits set by the Federal Reserve. The proposed regulations call for a much more narrow definition of "rural or underserved" than is dictated by the Dodd Frank Act.

If the definition remains as proposed, AgStar believes the likelihood of new lenders entering these "rural or underserved" markets to provide alternatives to existing lenders, particularly smaller and locally owned or managed lenders, will significantly decrease. Additionally, most lenders are pleased if the escrow services that they are required to provide break even from a cost perspective. Therefore, any new requirements that place additional financial burdens on lenders, will undoubtedly result in lenders reevaluating whether they even wish to provide options to consumers that would require them to take on these additional administrative expenses. If lenders chose to stop providing these products, many consumers will be unable to find mortgage products for which they qualify and they will remain under-served.

The proposed regulations provide for the exemption from the additional escrow functions if:

1. 50% or more of its HPMLs were made in counties designated by the Federal Reserve as rural or underserved;
2. During either of the preceding two years the lender originated and retained servicing to 100 or fewer first lien mortgage loans; and
3. The lender and its affiliates do not maintain escrow accounts for other home loans.

AgStar encourages the Federal Reserve to consider modifications to each of these three "tests" in any final regulation that may be promulgated. We are concerned that the very narrow exemption

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contemplated by the proposed regulations will significantly disrupt home mortgage lending in rural communities.

As part of the first test, the Federal Reserve is using what we believe is an exceedingly narrow definition of "rural." The proposed regulation identifies counties as "rural" only if they fall within one of four "urban influence codes" utilized by the Economic Research Service of the United States Department of Agriculture ("USDA"). The narrowness of this definition is evidenced by the fact that in the two states that make up AgStar's local service area – Minnesota and Wisconsin – only 18 counties in Minnesota and 12 counties in Wisconsin would meet the definition of rural. Both states are predominately rural, and the definition should be broadened as it fails to encompass large areas of each state that are clearly rural. Indeed, USDA itself utilizes various definitions of "rural" depending on the context and purpose of the definition of being areas with populations of 2,500 to areas with populations of 50,000.

The second test (100 or more loans) does not provide sufficient volume for a lender to ensure that it can escrow in a cost-effective manner, and such a small volume is in no way mandated by the Dodd Frank Act. The costs associated with setting up a system and processes and with staffing are significant and can only be made "cost-effective" if there is significant volume. AgStar believes that a more appropriate figure would be that a lender originating and servicing 1000 or fewer loans annually could still qualify for the exemption. Setting the limit at this level would increase the likelihood that only lenders with the type of volume that can make escrowing cost-effective are required to do so.

The third test may also prove problematic. At a minimum, it should be clarified that a lender who may presently only require occasional escrows for distressed loans are still eligible for the exemption. There may be circumstances where a lender is working with a distressed borrower and is seeking to avoid foreclosure. As part of the ongoing servicing of the loan, the lender could potentially require that certain costs be escrowed until the borrower and his or her loan are no longer distressed. In these situations, some lenders have elevated servicing and a lender that would otherwise qualify for the exemption should not be "penalized" because it chooses to attempt to resolve distressed loans in ways other than foreclosure.

We would also encourage the Federal Reserve to explicitly authorize what is implicit in the proposed regulation related to timing of the disclosures. Namely, Section 226.19(f)(1) provides that the disclosures must be "separate from all other material." AgStar interprets that provision as not requiring a lender to provide the escrow disclosure as part of a separate mailing or other delivery to the consumer. Instead, if a lender chose to, it could provide any required escrow disclosure to a consumer along with other information provided to the consumer prior to the consummation of the loan as long as (1) the three day time period was met and (2) the disclosure was made on a separate document from any other information. AgStar believes that clarifying

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this provision as part of any final regulation would enhance lender compliance with this requirement.

Again, thank you for the opportunity to comment on the proposed regulations. Feel free to contact me if you have any questions.

Sincerely,



Jodie Hermer  
Vice President, Home Mortgage Services