NYRL

NEW YORKERS FOR RESPONSIBLE LENDING

c/o NEDAP / 176 Grand Street / New York, NY / 10013
Tel: (212) 680-5100 / Fax: (212) 680-5104 / nyrl@nedap.org

July 22, 2011

Jennifer J. Johnson
Secretary, Board of Governors of the Federal Reserve System
20th Street and Constitution, Avenue NW
Washington DC 20551
Via email: regs.comments@federalreserve.gov

RE: Docket No. R-1417 and RIN No. 7100-AD75, Proposed Rule Amending Regulation Z and Expanding the Ability-to-Repay Requirement

To Whom It May Concern:

The 50 undersigned members of the New Yorkers for Responsible Lending coalition submit the following comments on the proposed regulations to amend Regulation Z to expand the scope of the ability-to-repay requirement, as mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act. We thank the Federal Reserve Board for the opportunity to comment on these critical regulations. We request that the Board consider this comment letter to constitute 50 separate letters for the purposes of counting the total comments received on this proposal.

New Yorkers for Responsible Lending (NYRL) is a 154-member state-wide coalition that promotes access to fair and affordable financial services and the preservation of assets for all New Yorkers and their communities. NYRL members represent community financial institutions, community-based organizations, affordable housing groups, advocates for seniors, legal services organizations, and community reinvestment, fair lending, and consumer advocacy groups.

Our groups have pushed for many years for comprehensive and sensible federal rules on underwriting. During that time period, abusive lending practices were rampant, devastating low- and moderate-income communities and communities of color throughout New York State, and displacing hundreds of thousands of families. The hallmark of these abusive lending practices were loans that were unaffordable from their inception, and that were based on the value of the property rather than on the family's ability-to-repay. New York was one of the first states to pass responsible lending legislation requiring verification of the ability-to-repay, but the effect of the state law was severely limited by federal preemption.

Given the importance of the current rulemaking in protecting consumers from abusive loans, the undersigned NYRL members urge the Federal Reserve Board and, subsequently, the Consumer

Financial Protection Bureau (CFPB), to implement the strongest, most robust regulations possible. We appreciate the approach the Board has taken to implement the expanded ability-to-repay requirement to provide specific criteria as well as much-needed flexibility. We believe, however, that the proposal could be strengthened in several ways to provide additional assurance that borrowers are protected from unaffordable, high-risk loans. Most important, the Board must not provide a safe harbor for lenders with respect to the ability-to-repay requirement.

Qualified Mortgages Must Provide a Rebuttable Presumption of Compliance, Not a Safe Harbor for Lenders

In its proposed regulations, the Board presents two alternatives for a "qualified mortgage" under Dodd-Frank. Under Alternative 1, the factors enumerated in the statute are sufficient to define a loan as a Qualified Mortgage and to establish a safe harbor for the lender. This would effectively mean that the lender or assignee is entitled to an irrefutable presumption that it has complied with Dodd-Frank's ability-to-repay standards without having to actually comply with the general ability-to-repay standards proposed by the Board.

We are deeply concerned with the approach outlined in Alternative 1. Given the years of rampant falsification of income and intentionally shoddy underwriting by the industry, a safe harbor based on the lender's mere assertion that it has verified income and assets would open the door to continued abuse. The safe harbor would deprive the borrower of critical defenses to foreclosure, even where the creditor did not make a good faith determination of the borrower's ability-to-repay. This interpretation would undermine Congress' clear intent in Dodd-Frank in mandating a defense to foreclosure for violations of the Act.

Instead, we urge the Board to use Alternative 2 in defining a Qualified Mortgage. A rebuttable presumption would not shield a lender from legal liability if the borrower can establish that the lender did not make a reasonable determination of her ability-to-repay. The additional underwriting requirements in Alternative 2 would require lenders to actually underwrite loans. In addition to the factors listed in the statute, a creditor would also have to include in its underwriting: employment status, simultaneous liens, current debt obligations, debt-to-income ratios or residual income and credit history. These additional factors are essential to a creditor's ability to accurately determine ability to repay, and must be included as a requirement for a Qualified Mortgage.

In sum, the limited ability-to-pay standards in Alternative 1 would open the door to abuse by unscrupulous lenders, and the safe harbor would fuel abusive lending since borrowers would have little legal recourse. In contrast, Alternative 2 would provide substantially better protections for borrowers as well as sorely needed safeguards against widespread risky lending.

A Strong Ability-to-Repay Standard Is Critical to Preventing Lending Abuses

Consistent with Dodd-Frank, the Board has proposed eight underwriting factors to determine a borrower's ability to repay, including current or reasonably expected income and assets; employment status; monthly mortgage payments including payments on any simultaneous loan; monthly mortgage-related obligations; current debt obligations; debt-to-income ratio or residual income; and credit history. While we generally support the rigorous standards that the Board has proposed, we have several concerns and suggestions.

Credit reports and credit scores as provided by the major credit bureaus often reflect discrimination
While a borrower's credit history can be relevant in determining ability-to-repay, the use of credit reports and credit scores often reflects past discrimination and adversely impacts people of color in particular. For years, communities of color have been redlined by mainstream banks and targeted for unaffordable mortgages and other abusive credit products. The high price of credit and financial services in communities of color has had a devastating effect on peoples' credit, but the damaged credit history may not reflect a borrower's willingness or ability to afford a fairly priced loan. The Board's new lending standards should not perpetuate years of discrimination by over-emphasizing the use of traditional credit history, in particular credit scores. At the very least, the Board should require that lenders look at other underwriting factors first, and that borrowers be given an opportunity to explain a negative credit history before they are denied a loan based primarily on this factor.

The payment calculation should be based on the maximum rate or interest rate cap, whichever is greater
Under the general ability-to-repay standard, the Board proposes that the payment calculation be made using the fully indexed rate of the loan (the rate as of the date the loan is made plus the maximum margin) or the introductory rate, whichever is greater. We are concerned that over time, and particularly during times of economic stress, there can be substantial volatility in mortgage interest rate indices such as LIBOR, which could cause significant payment shocks. Therefore, we urge the Board to use its exception authority to change the payment calculation to one using the maximum rate or the interest rate cap, whichever is greater, rather than the fully indexed rate.

The definition of "simultaneous liens" should be clarified
Since abusive home equity lines of credit (HELOCs) were widespread leading up to the crisis, we are pleased that the Federal Reserve used its discretionary authority to add HELOCs as one type of simultaneous lien a lender must consider.

In the final rules, however, we urge the Board to clarify that simultaneous liens, including HELOCs, should be included in the underwriting calculation for both refinance and purchase money mortgages. NYRL includes many organizations that provide foreclosure prevention counseling and legal services, and they have seen first-hand that unaffordable second liens, whether originated alongside a home purchase or as a refinance loan, can easily push homeowners into foreclosure.

The Board should tighten the standard for debt-to-income ratios
In the proposed rules, the Board proposes that the debt-to-income ratio be based upon Federal Housing Administration (FHA) standards or other widely accepted nongovernmental standards. We are concerned that the "widely accepted nongovernmental standards" could be similar to the loose standards some lenders used in the run-up to the financial crash to gouge borrowers. We urge the Board to include in its final rule that only loans following debt-to-income standards

sanctioned by the FHA, Fannie Mae or Freddie Mac, constitute Qualified Mortgages and are therefore in compliance with the ability-to-repay requirement.

The Board should require lenders to consider non-debt recurring obligations or expenses in determining ability-to-repay

Many families have recurring obligations, such as child care expenses or health insurance premiums, which significantly impact the borrower's ability to repay but are not considered "debts" for purposes of underwriting. Lenders should be required to consider these recurring obligations in considering a borrower's actual ability to repay a loan.

The payment calculation for balloon loans should be based on a longer term

For underwriting higher-priced balloon loans, the Board proposes that the payment calculation use the maximum payment in the schedule, including the balloon payment. As the Board states, this will effectively limit higher-priced balloon loans to only affluent consumers with substantial assets.

However, for balloon loans that are not higher-priced, the Federal Reserve proposes that the payment calculation use the maximum payment scheduled during the first five years after origination. The Federal Reserve rationalizes the five year time frame by saying the time frame is consistent with other aspects of Dodd-Frank. Balloon loans were abused repeatedly during the years of heavy subprime lending. In order to avoid repeat episodes, the time period for the payment calculation in an ability-to-repay analysis for balloon loans should be increased to ten years.

Additional Suggestions

The Board should clarify that the provisions for refinancing a non-standard mortgage should also apply to borrowers whose rates have already re-set

As the Board notes, Dodd-Frank encourages creditors to refinance borrowers out of hybrid mortgages that pose payment shocks, into lower-cost standard mortgages. Dodd-Frank does not appear to limit this refinancing option to non-standard loans that have yet to recast. We urge the Board to clarify that this refinance option is available to borrowers who have remained current on their loans even after an interest rate reset or after hitting the negative amortization limit on their loans, as long as the other requirements hold. These borrowers may be even better credit risks than those whose loans have not recast, and they would clearly benefit from a materially lower monthly mortgage payment.

The points and fees definition for Qualified Mortgages should not include any additional loopholes

The Board requests comment on whether points charged – to meet risk-based pricing adjustment requirements in the secondary market or to offset loan-level risks on loans held in portfolio – should be excluded from the 3% cap on points and fees for Qualified Mortgages. Excluding risk-based pricing adjustments from the points and fees cap would narrow the definition of points and fees well beyond any existing Federal or State law, and would open a substantial loophole for price gouging and abuse by lenders. We strongly urge the Board not to provide any additional loopholes for lenders in the definition of points and fees.

The Board should not allow lenders to categorize certain balloon loans as Qualified Mortgages
Dodd-Frank enables the Board to allow banks serving rural or underserved areas to include certain balloon loans as qualified mortgages, but the Act does not mandate the exception. In the proposal, the Board states that in order to preserve access to credit in rural and underserved areas and to allow smaller community banks to hedge against interest rate risk, it is allowing banks with assets under $2 billion to label certain portfolio-held balloon loans as Qualified Mortgages. We urge the Board to abandon this proposal at this time. First, widespread abuses were associated with balloon loans in the years leading up to the financial crisis. Secondly, the proposal does not present any evidence that preserving access to balloon loans is critical in assuring access to credit in rural and underserved areas. Before a new rule is proposed, the CFPB should investigate whether balloon loans issued by community banks are in fact critical for access to credit for rural communities.

The use of ARMs in the Standard Mortgage definition should be limited
We support the Board's definition of a "standard mortgage" as a covered transaction which does not contain negative amortization, interest-only payments, or balloon payments. However, we believe that the Board should limit the use of ARMs in the Standard Mortgage definition. Although ARMs existed long before the ongoing mortgage crisis, they played a major role in the subprime lending boom and the financial meltdown that followed. ARMs were used in loan flipping schemes that trapped borrowers in unaffordable loans with no option but to refinance into even less affordable mortgages.

In low and moderate interest rate environments, most borrowers will be better served by a fixed rate mortgage. Although some borrowers may not be able to afford fixed rate loan payments but may be able to afford slightly lower adjustable rate mortgage payments, those borrowers are unlikely to be able to afford even a small interest rate reset. We urge the Board to consider limiting Standard Mortgages to fixed and step rate loans, and 5/25s or longer term ARMs in low and moderate interest rate environments. In high interest rate environments, an ARM could potentially reduce borrowers' monthly payments substantially at reset, a feature that may outweigh the risks of increased payments for some borrowers. The Board should therefore consider allowing shorter term ARMs, such as 2/28s, to serve as Standard Mortgages in high interest rate environments only.

The payment calculation period for Qualified Mortgages should be extended
For Qualified Mortgages, the Federal Reserve proposes that the underwriting payment calculation be based on the maximum interest rate that may apply during the first five years after origination. This will put caps on interest rates that lenders charge for the first five years. We are concerned, however, that five years may not be long enough to assure ability-to-repay given that the average homeowner in the United States holds her mortgage for approximately seven years – a figure that will likely increase as abusive refinance practices are restricted. We urge the Board to consider extending the time period for the payment calculation for Qualified Mortgages to the average mortgage duration or the first 10 years.

Conclusion

Dodd-Frank's ability-to-repay requirements provide a long-awaited and much-needed framework to protect borrowers and communities from abusive lending practices. It is critical that the Board keep this goal in mind while implementing the final rule. If you have any questions, please do not hesitate to contact Josh Zinner of NEDAP (212-680-5100), Hubert Van Tol of PathStone (585-340-3324), or Barb van Kerkhove of Empire Justice Center (585-295-5815).

Sincerely,

ANHD, INC.
Arbor Housing and Development
Brooklyn Cooperative Federal Credit Union
Brooklyn Housing and Family Services
CAMBA Legal Services, Inc.
Chhaya CDC
Common Cause/ NY
Community Development Corporation of Long Island
Community Housing Innovations, Inc.
Cypress Hills Local Development Corporation
District Council 37, AFSCME
Elder Law Clinic, St. John's University School of Law
Ellicott District Community Development, Inc.
Empire Justice Center
Fair Housing Council of Central New York State, Inc.
Fifth Avenue Committee
Flatbush Development Corporation
Greater Rochester Community Reinvestment Coalition
Grow Brooklyn
Health and Welfare Council of Long Island
Housing Court Answers, Inc.
Housing Resources of Columbia County
JASA/Legal Services for the Elderly in Queens
Legal Services for the Elderly, Disabled or Disadvantaged of Western New York, Inc.
Legal Services NYC
Legal Services NYC -- Bronx
Long Island Housing Services, Inc.
Margert Community Corporation
MHANY Management, Inc.
MFY Legal Services
Nassau/Suffolk Law Services
NEDAP
Neighbors Helping Neighbors
Neighborhood Housing Services of New York City, Inc.
Neighborhood Preservation Coalition of New York State, Inc.

NeighborWorks Alliance of NYS
New York Public Interest Research Group
Parodneck Foundation
PathStone
Pratt Area Community Council
Queens Legal Services
South Brooklyn Legal Services
Staten Island Legal Services
The Financial Clinic
The Housing Council
The Legal Aid Society
Troy Rehabilitation and Improvement Program, Inc. (TRIP)
University Neighborhood Housing Program
West Harlem Group Assistance, Inc.
Westchester Residential Opportunities, Inc.

cc: Consumer Financial Protection Bureau