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MEMORANDUM

TO: Public File

FROM: Karen Osterloh, Assistant Chief Counsel

DATE: May 10, 2002

RE: Alternative Mortgage Transaction Parity Act; Preemption
Proposed Rule – Docket No. 2002-17
Summary of OTS meeting with members of the public

Attendees

On May 1, 2002, the following individuals met at OTS headquarters in Washington, DC:

- Members of the public – Mr. Joseph T. Lynyak III., Buchalter Nemer Fields & Younger, Los Angeles, CA (representing the California Mortgage Bankers Association and various state-chartered savings associations); and Ms. Lauren G. Delehey, Reed Smith, LLP, Princeton, NJ (representing a number of independent state housing creditors).

- OTS – Teresa Stark, Senior Project Manager, Compliance Policy; and Karen Osterloh, Assistant Chief Counsel.

Summary of Discussion

Mr. Lynyak indicated that he and Ms. Delehey have various legal and policy concerns regarding the proposed rule. They also have a suggestion for an alternative approach.

Mr. Lynyak raised the following legal concern. In Mr. Lynyak's view, the Parity Act requires a "top down" approach, which limits OTS discretion. Under this approach, OTS must first define alternative mortgage transactions. Once it defines these transactions, however, OTS must apply all rules that apply to a federal thrift's alternative mortgage transactions to a state housing creditor's transactions. In other words, if a federal savings association may engage in an alternative mortgage transaction, a state housing creditor must be able to make the same loan under the same terms. He argued that there must be true parity and that OTS may not create any disparity in the treatment of federal thrifts and state housing creditors.

Ms. Osterloh asked whether this is the sole issue. She noted that OTS regulations preempt various state lending laws for federal thrifts. These state laws address may address such matters as terms of credit, loan-related fees, points, servicing fees, and other items. Must OTS apply these rules to state housing creditors under the Parity Act?

Mr. Lynyak indicated that if the federal law addresses one of the terms of the loan as reflected in the loan documents, the answer is yes.

Mr. Lynyak emphasized that state housing creditors operating on a national or regional basis must comply with a growing number of complex state lending laws, and that adherence to these laws adds to costs and compliance burdens. He observed that the laws in 51 states not only differ from one another, but that laws within an individual state may apply different restrictions to different types of loans.

Ms. Delehey noted that the position expressed in the proposed rule would raise issues in the litigation of claims under the Parity Act. She noted that federal cases (Face and Shinn) have consistently held that the Parity Act was intended to provide state housing creditors with parity with federal thrifts – on the same terms as federal thrifts. These cases did not focus on whether the application of an OTS regulation was "necessary" to provide parity. She noted that if the proposed rule were finalized, litigation would become more fact-based.

Ms. Delehey also noted that the Parity Act regulation does not define or limit the scope of Parity Act preemption. (The Parity Act itself does that by stating that its purpose is to place non-federally chartered housing creditors offering alternative mortgage transactions on par with federal institutions offering such transactions.) Rather, the regulation defines which OTS regulations a non-federally chartered housing creditor offering alternative mortgages must follow to benefit from Parity Act preemption. The proposed revision would remove the prepayment and late fee regulations from that list. Ms. Delehey observed that the proposed rule would not have the effect that the OTS argues. I.e., the rule would not change the express preemption established by the Parity Act itself, removing a particular portion of the alternative mortgage transaction from the Act's preemption. Rather its effect would only be to say that a non-federally chartered housing creditor would not be required to follow those particular federal regulations in order to claim federal preemption. This may have been clearer when the Parity Act was implemented, as the referenced payment and late fee provisions contained direct limits on such fees.

Mr. Lynyak expressed several policy concerns. First, he argued that the proposed rule could create a "schizophrenic" treatment of operating subsidiaries of federal thrifts. He asked whether operating subsidiaries making alternative mortgage transactions would have the benefits of federal preemption to the same extent as federal thrifts. Or would operating subsidiaries only have preemption benefits under the Parity Act regulation? He noted that this issue must be clarified or litigation may follow.

Second, he warned that OTS statements on Parity Act preemption may undermine its position on preemption under the HOLA. Specifically, he cautioned that some statements made with respect to Parity Act preemption could be applied in cases involving federal preemption under the HOLA and could diminish the value of the federal thrift charter.

As an alternative to the proposed rule, Mr. Lynyak suggested that OTS should consider imposing various caps on a federal thrift's ability to impose prepayment penalties and/or late fees, and then apply these caps to state housing creditors through the Parity Act regulation. He noted that this alternative would require further discussions and an analysis of the caps that are generally imposed in the industry. Mr. Lynyak indicated that several large thrifts that purchase loans from state housing creditors are currently considering whether they would favor a more restrictive regulatory environment.

Ms. Osterloh indicated that such an alternative would require additional notice and comment under the Administrative Procedure Act.

Ms. Stark inquired whether this alternative would also undermine the thrift charter.

Mr. Lynyak responded that commercial banks and credit unions do not engage in home lending to the same extent as savings associations. This should not be an issue for the vast majority of lending institutions.

Ms. Osterloh asked whether he was aware of any sources of information regarding standard industry practices regarding prepayment penalties.

Mr. Lynyak indicated that there were several sources of information including the Harvard Center for Housing Studies. He also indicated that thrift trade associations might have such information available. He suggested that OTS initiate a dialogue with thrifts in advance of any rulemaking proposing his alternative. Mr. Lynyak further indicated that his clients were very interested in the proposed rulemaking and would provide additional information, if OTS believes that this would be constructive.