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United States Senate
COMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS
WASHINGTON, DC 20510-6075

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July 26, 2002

Honorable James Gilleran
Director
Office of Thrift Supervision
1700 G Street, N.W.
Washington, D.C. 20552

Dear Director Gilleran:

The Office of Thrift Supervision ("OTS") recently published proposed changes in the regulations governing the Alternative Mortgage Transaction Parity Act ("Parity Act") [Docket No. 2002-17]. I believe that the proposal to amend § 560.220 of the OTS regulations represents a major step forward in the fight against predatory mortgage lending and should be adopted by the OTS.

I understand that the OTS's proposal was made after a careful review of the agency's current regulations and extensive public comments received in response to the April 5, 2000 advanced notice of proposed rule making. I commend you for your decision to close a loophole that permits state housing creditors to evade state laws aimed at protecting consumers from unfair prepayment penalties and late fees simply by structuring mortgages as variable rate loans. The proposed changes clearly reflect serious consideration of the issue.

Predatory mortgage lending has been on the rise in recent years. As you know, the Banking Committee is closely examining the problem. The Banking Committee held a number of hearings on predatory mortgage lending and heard from victims of predatory lending as well as a broad array of witnesses representing consumer, community, and industry interests. These witnesses detailed stories of lending characterized by very high interest rate loans, high up-front fees financed into the loan, and egregious prepayment penalties which prevent borrowers from refinancing into lower rate loans with other lenders. These practices strip equity from homes and can often lead to foreclosure. There are virtually no limits on the charging of prepayment fees under Federal law. However, numerous states have enacted legislation restricting abusive and exorbitant prepayment penalties and late fees. Unfortunately, some state housing creditors are using the Parity Act's preemption authority to circumvent states laws aimed at protecting homeowners by restricting these practices.

Therefore, I strongly support the OTS's proposal to delete § 560.34 (prepayment penalties) and § 560.33 (late fees) from the list of OTS regulations designated for alternative mortgages that preempt state law. The proposal is consistent with the purpose of the Parity Act and will improve the ability of states to protect consumers from abusive equity stripping lending practices.

The Parity Act is intended to encourage non-federally chartered lenders to make alternative mortgages by preempting state laws that prohibit these lenders from offering adjustable rate mortgages. The Parity Act was enacted during the mortgage crisis of the early 1980s when many states prohibited lenders from originating loans other than conventional fixed-rate mortgages. The OTS, and other federal banking regulators, issued regulations permitting federal thrifts to originate variable rate mortgages and other "alternative" mortgages notwithstanding state law in order to stimulate the availability of credit. Congress passed the Parity Act to insure that state housing creditors would also be permitted to offer alternative mortgages. The law makes clear that the purpose of the Parity Act is to "prevent discrimination against State-chartered depository institutions, and other nonfederally chartered housing creditors, with respect to the making, purchasing, and enforcing alternative mortgage transactions." 12 U.S.C. § 3803(a), emphasis added.

The Parity Act assigns the OTS with the responsibility to determine which of its federal thrift "alternative mortgage" regulations it will allow state chartered thrifts and finance companies to utilize to preempt state law. Until 1996, the OTS consistently interpreted the Parity Act's preemption authority to only apply to state laws targeted exclusively at the ability to make alternative mortgages. Only terms that are intrinsic to the ability of a state housing creditor to offer alternative mortgages were listed in the OTS regulations that preempt state law. For example, Federal regulations related to adjustments in home loans and disclosures for variable rate transactions could be used to preempt state law. Federal thrift regulations that also applied to conventional mortgage loans were deemed inappropriate for state housing creditors because they are not an integral part of, or particular to, alternative mortgage transactions.

I believe that the OTS erred in 1996 when it added prepayment penalties and late fees to the list of OTS regulations that preempt state law and expanded the Parity Act's preemption authority beyond those elements essential to the ability to offer alternative mortgages. Neither the legislative history nor statutory language of the Act supports the interpretation contained in the OTS's 1996 overly broad legal opinion. The purpose of the Parity Act is to prevent state housing creditors from being prohibited from making alternative mortgages where Federal chartered institutions could do so. The Parity Act preserves the authority of states to regulate loan terms applicable to conventional loans made by state chartered lenders.

I agree with the preamble to the proposed rule that prepayment penalties and late fees regulations are not "essential to enable housing creditors to continue to provide alternative mortgages" and "apply to real estate loans in general." Accordingly, I believe that these provisions should be removed from the list of regulations state housing creditors can use to preempt state laws.

With respect to application of this proposal to all state housing creditors, I do not believe that the OTS should draw a distinction between state-chartered depository and non-depository institutions. State-chartered depository institutions are creatures of state law and should therefore abide by the laws of the state in which they are chartered.

I support the proposal and believe that it will enable states to better regulate state-chartered thrifts and finance companies. I appreciate your consideration of my views on this important proposal.

Sincerely,

A handwritten signature in black ink, appearing to read "Paul Sarbanes". The signature is fluid and cursive, with a long horizontal stroke extending to the left.

Paul S. Sarbanes
Chairman
Committee on Banking, Housing and Urban Affairs